Pharmaceutical Sector
Selective Prescriptions

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Selective prescriptions

Multiple growth models

- **Generics**
  - **Generics business to improve gradually from 2006 onwards**
  - **Inorganic initiatives to gain scale – Indian companies better placed to extract value in long-term**
- **MNC Pharma**
  - **Portfolio realignment to drive growth in short-to-medium term**
  - **Patented products to drive long-term growth despite transfer pricing issues**
- **Contract Research & Manufacturing**
  - **India on the threshold of significant opportunity**
  - **Will have to be ready for long gestation periods**

Outlook

- **Generics – Safety is in large product baskets**
- **MNC Pharma – Parent's commitment will be a key determinant**
- **CRAMS – Customer relationships, IPR compliance and cost efficiencies are pre-requisites**

Recommendations

- **Generics – Ranbaxy, Cipla**
- **MNC Pharma – GSK Pharma**
- **CRAMS – Divi's Labs, Matrix, Nicholas Piramal**

Generics – Is the worst behind us?

Generics – is the worst behind us?

Generics

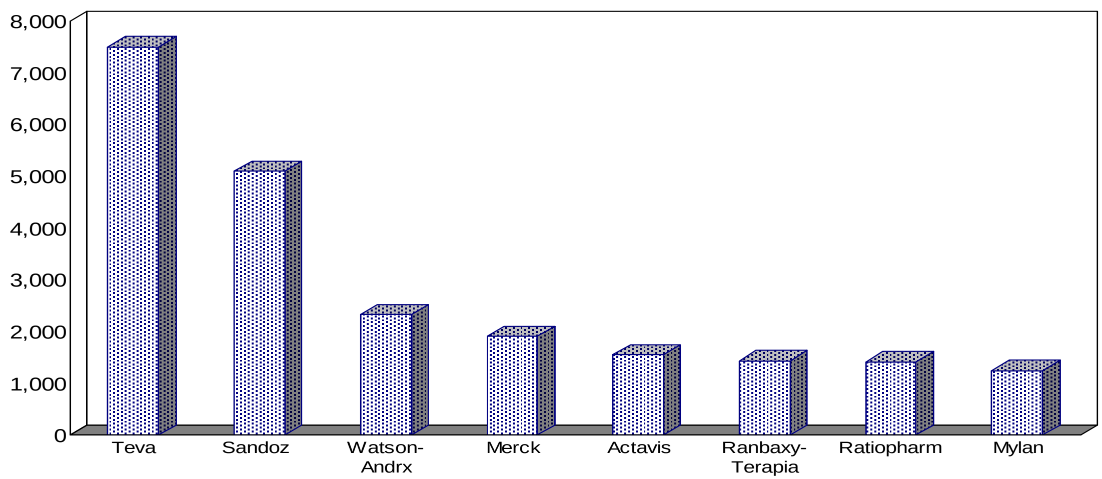
- **2005 was one of the worst years for generics**
  - **CY05 witnessed the twin impact of intense competition and very few new launches**
  - **Competition has intensified significantly – Aggressive filings from Indian companies**
  - **Innovators have adopted aggressive stance – Authorized generics, patent de-listing, defending IPRs vigorously**
  - **Shared 180-day exclusivities has diluted attractiveness of patent challenges**
- **What has changed over 2005?**
  - **CY06-07 to witness patent expiry worth $26b compared to $7b in CY05 leading to more new launches – takes care of one of key impediments for generics**
  - **Pricing to remain intensely competitive due to entry of more players & government pressures – However, further price deterioration unlikely as generic prices are already 5% of innovator price**
  - **Expect more consolidation as generics gain scale and expand geographical reach**
  - **Indian generic companies have initiated cost-cutting measures (including R&D hive-off)**
  - **Generics and innovators adopting a more pragmatic stance on patent litigations leading to settlements.**
  - **Governments worldwide trying to reduce healthcare costs – expect regulations to remain favorable.**

Generics – is the worst behind us?

Consolidation in the generic space

- **Increased competition leading to consolidation**
- **Acquire scale and expand product offerings**
- **Exploit backward-integration synergies in manufacturing**
- **Prevent competitors from entering/strengthening presence in key markets**
- **Indian companies better placed to extract value but recent stock price correction may impact ability to fund large acquisitions – However paybacks could be extended due to valuations**
- **Barring Teva and Ivax, rankings of generic companies likely to undergo significant change**

GLOBAL GENERIC RANKINGS (US $M)



Generics – is the worst behind us?

CONSOLIDATION IN THE GENERIC SPACE – MAJOR DEALS

ACQUIRER	ACQUIRED COMPANY	COUNTRY	ACQUISITION DATE	COST OF ACQUISITION (US$M)	EV/SALES (x)	EV/EBITDA (x)
Sandoz	Hexal & Eon	Hexal - Germany, Eon - USA	Feb-05	7,769	3.7	11.9
Matrix Labs	DocPharma	Belgium	Jun-05	238	2.0	17.4
Teva	Ivax	USA	Jul-05	7,400	3.3	24.6
Actavis	Alpharma	USA	Oct-05	810	1.0	10.4
Dr. Reddy's Labs	Betapharm	Germany	Feb-06	576	2.9	11.7
Watson	Andrx	USA	Mar-06	1,900	1.8	52.8
Actavis (proposed bid)	Pliva	Croatia	Mar-06	1,600	1.3	10.9
Ranbaxy	Terapia	Romania	Mar-06	324	4.1	11.6

Source: Companies/ Motilal Oswal Securities

Generics – is the worst behind us?

Generics – R&D hive-off to control costs

- **Leading generic companies like Dr. Reddy's Labs and Sun Pharma have de-risked their NCE & NDDS research**
- **Dr. Reddy's Labs has hived-off its NCE research into a JV**
- **Sun Pharma has proposed a de-merger of its NCE & NDDS research – savings of Rs3-4/share**
- **Ranbaxy yet to hive-off its NCE & NDDS research – potential savings of Rs2-3/share**
- **De-merger to help unlock value for NCE & NDDS research**

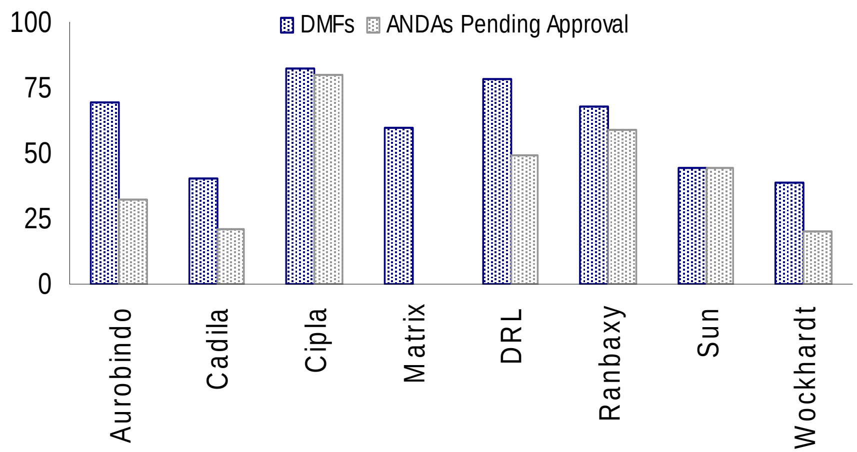
Generics – Pragmatic patent settlements

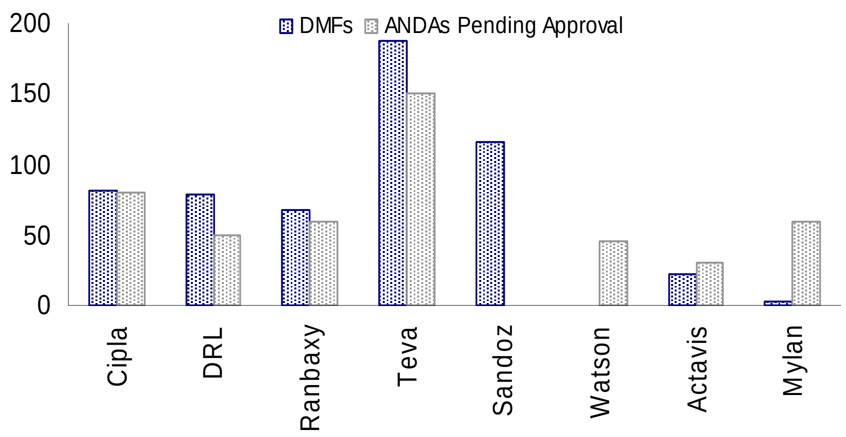
- **Sector has witnessed many out-of-court patent settlements, of late**
- **Innovators and generics taking pragmatic approaches to patent litigations**
- **Recent settlements include - Plavix (Sanofi-Apotex), Provigil (Cephalon-Teva and Ranbaxy), Lexapro (Forest-AlphaPharma), Effexor XR (Wyeth-Teva), Lamictal (GSK-Teva).**
- **Ranbaxy – Has 18 FTFs with Para-IV filings targeting about $14b in innovator sales**
- **DRL – Has 11-12 FTFs with Para-IV filings targeting about $10-11b in innovator sales**
- **Cipla – Partners likely to have filed some patent challenges (details not available)**

Generics – is the worst behind us?

Generics – India has one of the strongest generic pipelines

- **India accounts for about 25-30% of global DMF filings**
- **Indian companies ramping up pipelines aggressively with 15-20 DMFs and ANDAs targeted per year**
- **Most of global generic companies have started sourcing from India**
- **India's cost competitiveness and chemistry skills helping it to garner increasing share of the generic market – despite intense pricing pressure**
- **Given their competitive positioning, large Indian generic companies will be able to withstand the intense pricing pressures in generic market**





Generics – outlook

The worst is behind us

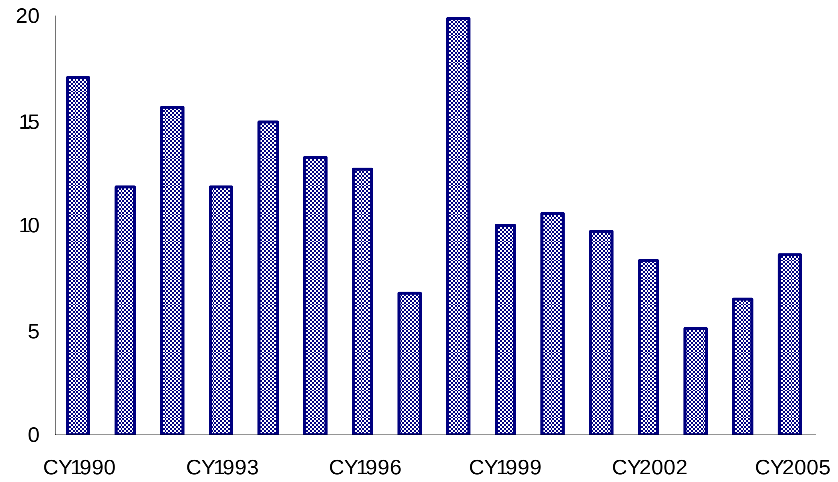
- **2005 was one of worst years for generics – expect improvement from 2006 onwards**
- **New launches, acquisitions to boost top-line**
- **Cost controls to have positive impact on margins**
- **India's cost competitiveness and chemistry skills will help sustain despite tough pricing scenario**
- **Large product portfolios and better scale of operations will help mitigate risks**
- **Expect more consolidation in the generic space to gain scale and enter new markets**
- **Acquisition multiple in generics space are still high – will extend paybacks for inorganic initiatives**
- **Indian companies better placed to leverage acquisitions given the possibility of shifting manufacturing back to India over the long-term**
- **Large Cap picks – Ranbaxy, Cipla**

MNC Pharma – Outlook post the IPR regime
Biggest Entry Barrier Created

Background: pre-2005 (pre-patent regime) scenario

- **Withdrawal of product patent protection in 1970 marked the beginning of the slide for pharma MNCs**
- **Indian arms of global companies were sandwiched between twin concerns**
  - **Reverse engineering and launch of their products by Indian companies, as no strong entry barrier remained**
  - **Few new product launches due to parents' lack of interest in the Indian operations**
- **Multiple players in every product led to commoditization of the market, as aggressive price competition and low-product differentiation took their toll**
- **MNC market share dropped from 70% to under 30% over the last 30 years, severely impacting growth rates and profitability**

INDUSTRY GROWTH RATES (%) - DIPPING CONSISTENTLY



MULTIPLE COPIES OF MNC PRODUCTS

DRUG	BRAND	PREM. OVER AVG PRICE	NO OF COPIES
Ramipril	Cardace	37	13
Glimepiride	Amaryl	130	15
Fexofenadine	Allegra	12	19
Dipyridamole	Clexane	119	1
Amoxycillin Comb	Augmentin	40	15
Betamethasone	Betnesol	11	9

Source: Industry/Inquire

Re-introduction of product patents - a harbinger of good times

- **Re-introduction of product patents via a presidential ordinance - BIGGEST ENTRY BARRIER HAS BEEN CREATED**
- **Despite lack of clarity on several issues and the possibility of modifications before the bill is passed, the intent to usher in product patents on time is a clear positive**
- **IPR protection is expected to encourage new product launches by MNCs and restrict pricing pressure in patented products**
- **Benefits would be substantial, although there could be some initial confusion over the law**
  - **Indian market to come under the radar of global companies as an attractive market**
  - **Greater willingness to launch more products (off patent), in a bid to build / strengthen franchise for more lucrative launches ahead**

Patents (Amendment) Ordinance 2004 – Highlights

- **Product patents extended to Pharmaceuticals; only new chemical entities to be patented**
- **Pre-grant and post-grant opposition provided for – timeline of 90 days set for ruling on pre-grant opposition**
- **Patent rights on mailbox applications to be granted only with prospective effect**
- **Compulsory license provisions retained to prevent misuse of patents / ensure availability in national emergency**

Clarity awaited on:

- **Data exclusivity provisions – to come out as a separate law**
- **Fate of mailbox applications – drugs that may have to be withdrawn by domestic companies**

Product patents – manifold benefits

- **Opens up a new 'patented' market with huge potential as incremental market of US$2-3b to be shared among 8-10 MNCs & their licensing partners**
- **Consolidation of existing market and dynamics of the existing market also to improve over time**
  - **Closing of the reverse engineering window for new products would make ability to build brands a key to success**
  - **Weaker players with limited branding/ marketing skills are expected to find it difficult to sustain, as their ability to copy and launch new products is hampered**
  - **Consolidation of prescription share among leading domestic and MNC companies expected – led by dropping out of weaker players**
  - **Marketing and brand-building will determine future success. MNCs would be more willing to put financial muscle behind key products**

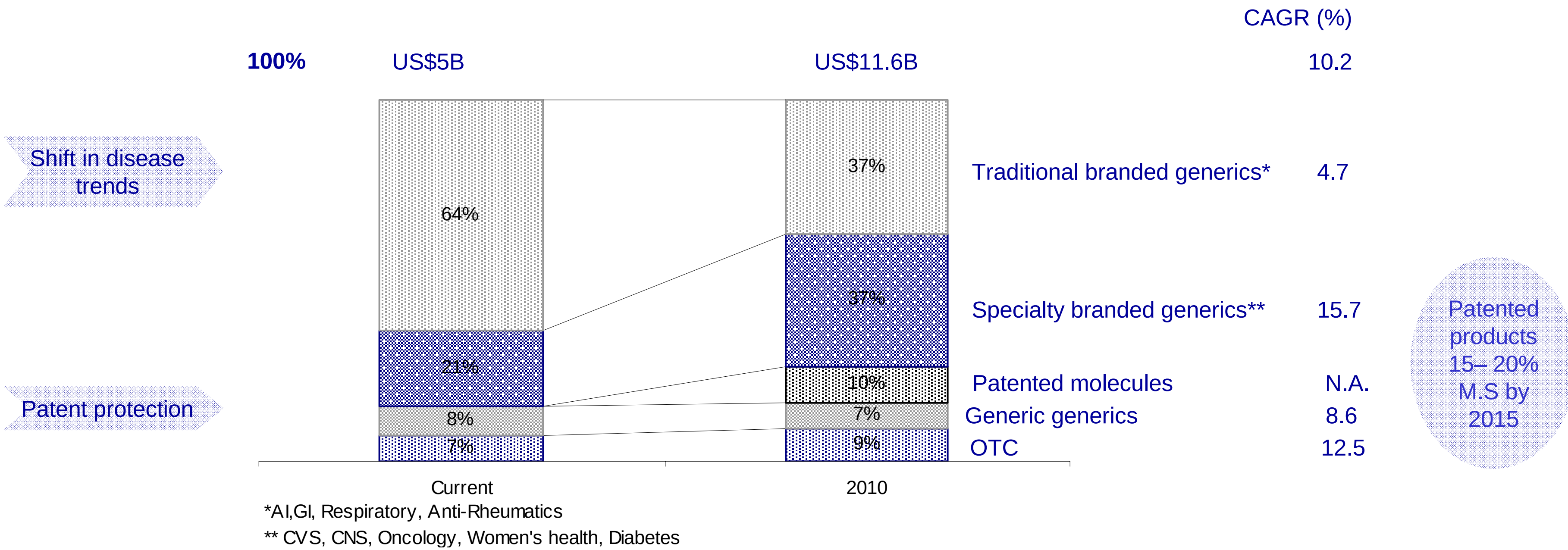
MNCs have superior branding ability

	MNC	India
Top 10	5	5
Top 20	8	13
Top 30	13	17
Top 40	16	24
Top 50	21	29

MNC brands dominate top-10 list

Brand	Company	Value (Rs m)	Rank
Voveran	Novartis	1,058	1
Corex	Pfizer	1,054	2
Phensedy	Nicholas	960	3
Taxim	Alkem	859	4
Becosules	Pfizer	790	5
Human mixtard	Abbott	770	6
Augmentin	GSK	766	7
Sporidex	Ranbaxy	752	8
Cifran	Ranbaxy	740	9
Asthalin	Cipla	740	10

Patented products will acquire significant market share



Source: GSK India

Product patents – bring in higher profitability in long-run

- **Despite enjoying monopoly, patented products may not have very high profit margins due to transfer pricing**
- **Patented products will have to offer significant therapeutic benefit over existing products**
- **Market potential is high for "RIGHT" product – AstraZeneca's Meronem could generate sales of Rs600m in 3rd year of launch due to absence of competition**
- **Consolidation in the "non-patented" market would also have a positive impact on margins**
- **Our hypothesis points to a 13% and 15% CAGR revenues and EBITDA over CY05-15**

- **The two key variables in our hypothesis are**
  - **Share of patented products in overall market-estimates range from 15-20% by 2015**
  - **Profitability of patent products for MNCs – Our estimates take care of the transfer pricing with the parent**

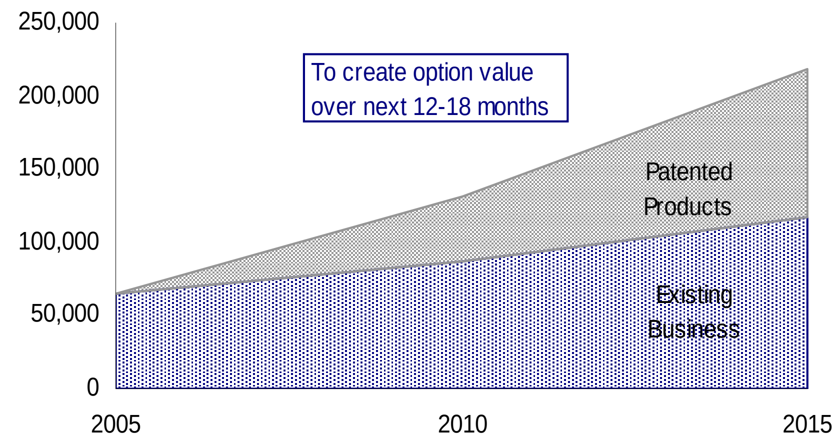
OUR HYPOTHESIS – A WHOLE NEW SEGMENT TO DRIVE GROWTH

(Rs.M)	2005	2010	*CAGR*	2015	*CAGR*
Market (US$b)	5	10	14.9%	15	11.6%
Market (Rs.m)	**225,000**	**450,000**	14.9%	**675,000**	**11.6%**
Proportion under patent (%)	0.0	10.0		15.0	
Patented sales	0	45,000	n.a.	101,250	n.a.
Generic sales	225,000	405,000	12.5%	573,750	9.8%
MNCs	**65,000**	**131,985**	**15.2%**	**217,655**	**12.8%**
current business	65,000	86,985	6.0%	116,405	6.0%
new business		45,000	n.a.	101,250	n.a.
EBIDTA	**16,000**	**39,595**	**19.9%**	**65,297**	**15.1%**
current business	16,000	26,095	10.3%	34,922	8.1%
new business (@ 30%)		13,500	n.a.	30,375	n.a.
EBIDTA margin (%)	*24.6*	*30.0*		*30.0*	

Product patent to create option value

- **Most MNCs have recorded excellent turnarounds over the last few years despite operating in very challenging conditions.**
- **We expect MNC Pharma companies to be able to record a steady 15-20% CAGR in earnings over the next few years, without any upside from product patents.**
- **Growth rates and profitability are expected to improve considerably over the next 5-10 years.**
- **Healthy bottom-line growth, along with steady dividend payouts and healthy return ratios are good enough to support current valuations.**
- **While tangible benefits from the new legislation would come in only two years down the line, valuations would start scaling up sooner.**
- **Potential upside from product patents would create 'Option Value' in MNC Pharma stocks over the next 12-18 months (a la generics opportunity for domestic companies)**
- **Our top pick is GSK Pharma**

BENEFIT OF PATENT REGIME TO CREATE OPTION VALUE



Benefits to come in long run, near-term scenario looks hazy

- **We expect some confusion in the market on account of the following factors**
  - **Debates and litigations on patentability – particularly with respect to products where patent filings have been done close to the 1995 deadline and have been introduced in the market by domestic companies**
  - **Status of drugs where EMRs have been filed in the mailbox**
- **We do not have any clarity on this front as yet and expect a lot of ambiguity and confrontation before things become clear. However, more clarity expected to come in, once the margin cases are dealt with and filing dates are unambiguous**
- **We believe, issues like DPCO, compulsory licensing etc. cannot mask the key positive – THE BIGGEST ENTRY BARRIER HAS BEEN CREATED BY IMPLEMENTATION OF IPRs**
- **Patented products are expected to be launched by MNC's from 2007/08 onwards. The product promotion is likely to begin at least 10-12 months before the actual launch of patented product. This has adversely impacted our estimates for CY07 with no commensurate revenue streams factored-in.**
- **The upside from patented products is susceptible to the success of the parent's R&D pipeline.**

Contrary to popular perceptions, India is attractive market

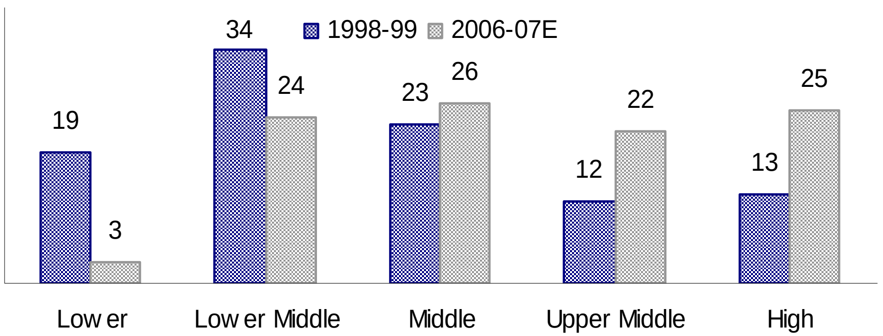
- **India is an attractive market for MNCs as**
  - **Large population**
  - **Limited penetration – only 30% have access to allopathic medicines**
- **Therapeutic mix moving in favor of lifestyle diseases - focus area of R&D for MNCs**
- **Premium pricing is possible in India**
  - **Lower pricing power in India is more a function of severe competition rather low ability/willingness to pay**
  - **Several instance of premium, yet India-friendly pricing exist in the market**
  - **Rising income levels and development of health insurance would add to the potential**
  - **About 40-50m people can afford the premium priced products and another 70-80m can afford products with moderate premiums**

EXAMPLES OF PREMIUM PRICING IN INDIAN MARKET

Brand	MS (%)	Premium over		No of
		Avg price (%)	Lowest price (%)	Competitors
Cardace (2.5mg)	27.1	36.8	354.8	23
Amaryl (1 mg)	4.6	124.9	453.8	34
Allegra (120mg)	6.5	43.6	109.2	19
Clexane (20mg)	28.2	55.9	130.0	11
Voveran (50mg)	10.2	56.7	328.6	33
Betnesol (0.5mg)	22.1	4.4	13.6	9

Source: Company/IDR/MOST

UPPER MIDDLE & HIGH INCOME HOUSEHOLDS TO GROW



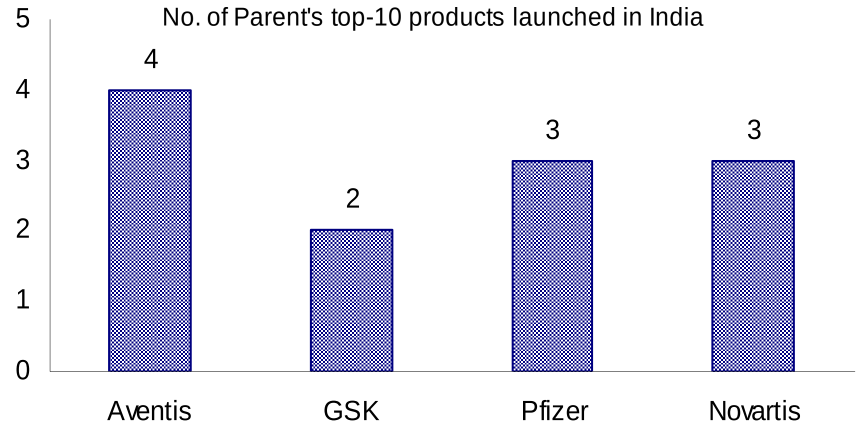
Slab definition at 01-02 prices - Low :<=$978 ; Lower Middle: $978-$1956; Middle:$1956-$2935; Upper Middle: $2935-$3804; High : >$3804

Source: NCAER

Portfolio mapping - upsides in short-to-medium term

- **Lack of patent protection and price control left very little incentive for MNCs to launch new products from their parents portfolio**
- **This led to an ageing product basket and therapeutic mix which was out of sync with parent's portfolio**
- **Leading MNCs have started rationalizing their portfolios by**
  - **Focusing on high growth and profitable brands**
  - **Mapping their therapy focus in line with their parents' focus areas**
- **Portfolio rationalization, leading to improved product mix, has been one of the factors driving profitability**

SIGNIFICANT OPPORTUNITY TO MAP PRODUCT PORTFOLIO WITH PARENT



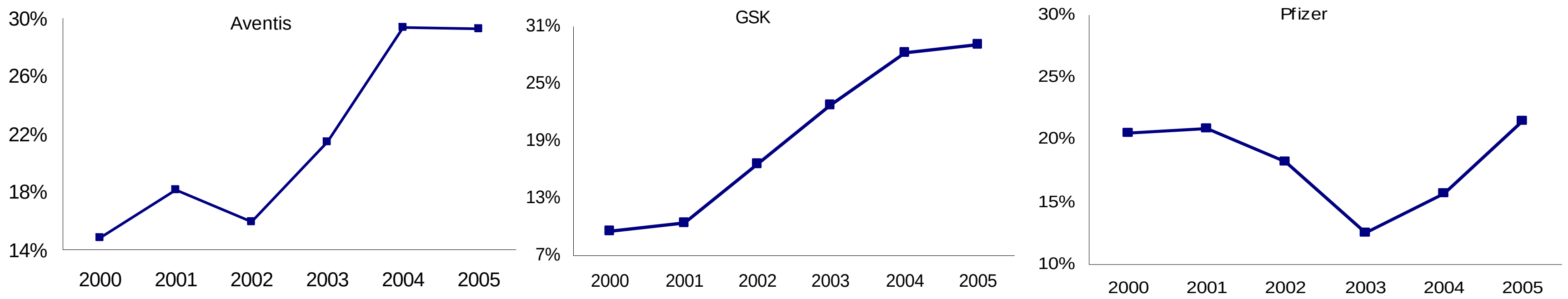
COMPARISON BETWEEN TOP PRODUCTS OF PARENT AND INDIAN ARM

	Parent	India
Aventis	Lovenox/Clexane	Rabipur
GSK	Seretide/Advair	Augmentin
Pfizer	Lipitor	Corex
Novartis	Diovan/Co-Diovan	Voveran

Benefits of cost cutting are behind us

- **MNCs have rationalized their cost structure significantly to cut all unnecessary costs and emerge as lean organizations**
- **Measure taken over the last few years include**
  - **Manpower rationalization (through VRS schemes)**
  - **Greater outsourcing and control over fixed overheads**
  - **Rationalization of fixed assets – manufacturing facilities, office property**
- **The combination of a better product mix and cost rationalization have seen EBITDA margins improve substantially**
- **Margins are expected to remain slightly muted in medium term as the companies start investing in promotion of patented products with no commensurate revenue flowing in**

EBITDA MARGINS REFLECTS BENEFITS OF COST CUTTING AND PRODUCT RATIONALIZATION



New Drug Policy will be a mixed bag

- **The New Drug Policy (proposed) has recommended the following proposals for the domestic pharmaceutical industry:**
  - **Raise the limit of profitability and post-manufacturing expenses a drug maker can claim from a price controlled drug from 100% to 150% of its ex-factory cost.**
  - **No change in the norm in the case of imported medicines, which now enjoy a 50% maximum allowable post-manufacturing expenses (MAPE).**
  - **Companies investing heavily in R&D and employing a particular number of scientists will be eligible for 200% MAPE.**
  - **The government's Essential Drug's List (consisting of 354 drugs) will form the universe of drugs which will attract some form of direct or indirect price controls.**
  - **Drugs with per pill cost of less than Re1 may not attract price controls.**
  - **About 39 drugs will attract price controls as per the existing DPCO norms compared to the current DPCO coverage of 74 drugs. However, these drugs will be eligible for the increased MAPE.**
  - **The remaining drugs in the Essential Drug's List (excluding some life-saving drugs) will attract ceiling prices to be determined by taking weighted average of the top three brands**
  - **The government will be devising a new formulae for computing prices of DPCO drugs and will do away with the current practice of fixing prices based on cost of manufacturing and market share**

Impact of proposed new drug policy

- **The revised norms may be a corrective measure by the regulatory authorities. Government will have to strike a balance between pragmatism on one hand and populist demands on the other. The change in norms of the DPCO (if implemented) may be the first step towards this. Our impact analysis indicates the following benefits to the Indian pharmaceutical industry, if the DPCO norms undergo a change:**
  - **DPCO products enjoying strong brand-equity will gain at the expenses of their competitors, despite price controls, due to the increase in MAPE.**
  - **Products falling outside the purview of price control (due to the Re1/pill norm) and having strong brand-equity will gain due to more pricing power.**
- **If the above norms are implemented in the same form, we expect some of the key products, like Combiflam (Aventis), Becosules (Pfizer), Zinetac (GSK), Human Mixtard (Abbott/Novo), Asthalin (Cipla), Cifran (Ranbaxy) etc, to gain pricing power.**
- **However, including all 354 drugs under price control (either DPCO or ceiling prices) may adversely impact the domestic operation of most of the pharmaceutical companies**
- <u>**It is important to note that these are only recommendations, pending the announcement of the final new drug policy. These recommendations may or may not undergo a change in the final policy.**</u>

Key risks/concerns

- **Risk of launching patented products through a 100% subsidiary**
  - **Most of the MNCs have at least one 100% subsidiary in India**
  - **This would maximize the profits from the patented products for the parent company**
  - **This could reduce the operational scope of the listed entity**
- **Transfer pricing for patented products would determine the profitability of the Indian arm**
  - **The price at which the parent would transfer patented product to its India arm would be the key determinant of profitability of the patented product to the Indian arm**
  - **The parent can capture most of the profits in its books by setting high transfer price, resulting in normal profits for the Indian arm**
- **Government Policies**
  - **Government may mandate negotiated pricing for patented products**
  - **Multiple pre-grant oppositions are being filed sequentially by different competitors for the same patent application. This leads to continuous and cyclical pre-grant opposition.**
  - **This leads to delay in granting a patent, thereby reducing the patent term that starts from the date of application.**

CRAMS – India on the threshold of a significant opportunity

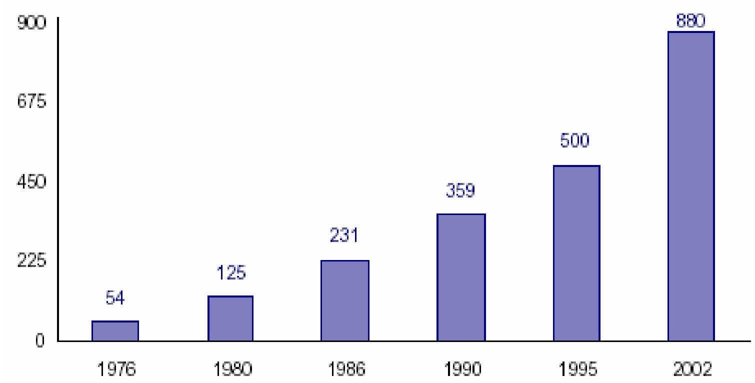
CRAMS - Opportunity

- **Outsourcing likely to gain steam as innovators start focusing on their core competencies i.e R&D and marketing due to rising cost pressures & low R&D productivity. MNCs to outsource "manufacturing"**
- **Unique combination of superior chemistry and regulatory skills, as well as good quality at low costs augurs well for India as a preferred outsourcing destination**
- **The contract manufacturing opportunity alone is likely to grow 10x to $1b by 2010 (i.e. 3-4% of global market opportunity)**
- **Given the high entry barriers, very few players in India are prepared to exploit this opportunity. We expect the top-5 players to get disproportionate share of business initially.**
- **Invest in resource-rich companies that can undertake the requisite front-ended capex and can deliver scale**
- **Investors should take long-term view on the CRAMS opportunity as gestation periods are likely to be longer and at times accompanied by phases of lower visibility**
- **Valuation and view**
  - **CRAMS opportunity is too large to ignore despite initial teething problems, which will be taken care of as Indian players strengthen their pipelines**
  - **Current valuations do not fully discount the stability of revenues and earnings that contract manufacturing is likely to entail in the long-term**
  - **Buy – Divi's Labs, Matrix, Nicholas Piramal**

CRAMS - Why outsource?

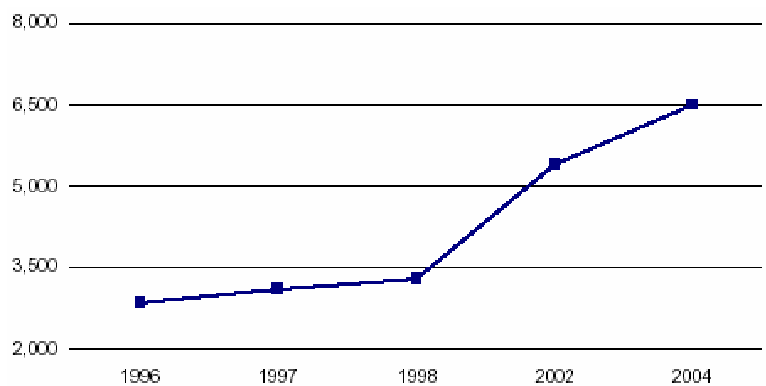
- **New drug development has become extremely time consuming taking at least 10-12 years**
- **Rate of new drug approvals is declining, with new molecule approvals CAGR of -6.5% (1996-2004)**
- **Cost of drug development is increasing (R&D investment CAGR is 11%)**
- **Fewer blockbuster drugs, competition from other patented products and intensifying generic competition, is leading to more drugs under development**
- **Hence, innovator pharmaceutical companies have started focusing on their core competencies (i.e. R&D and marketing) and are likely to out-source manufacturing**

RISING DRUG DEVELOPMENT COST (US$M/DRUG)



Source: Tufts

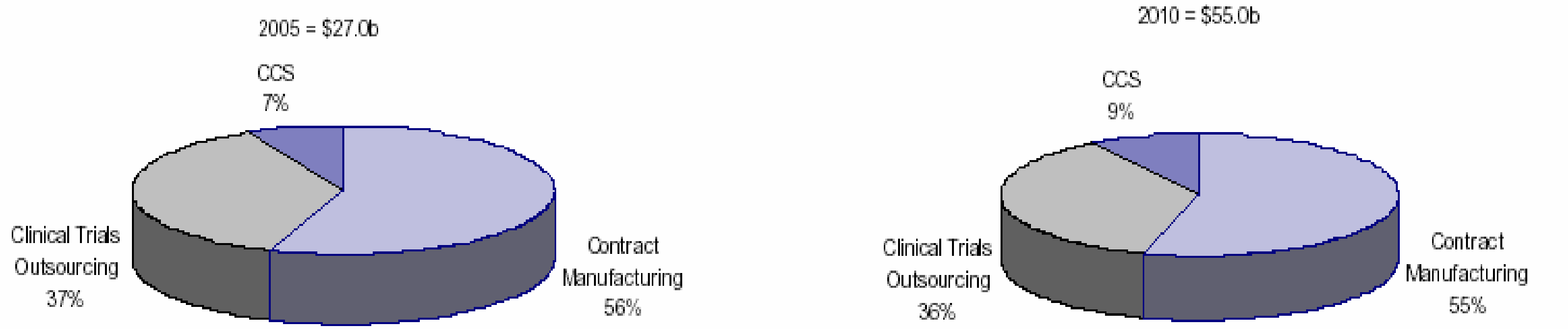
INCREASING NUMBER OF DRUGS UNDER DEVELOPMENT



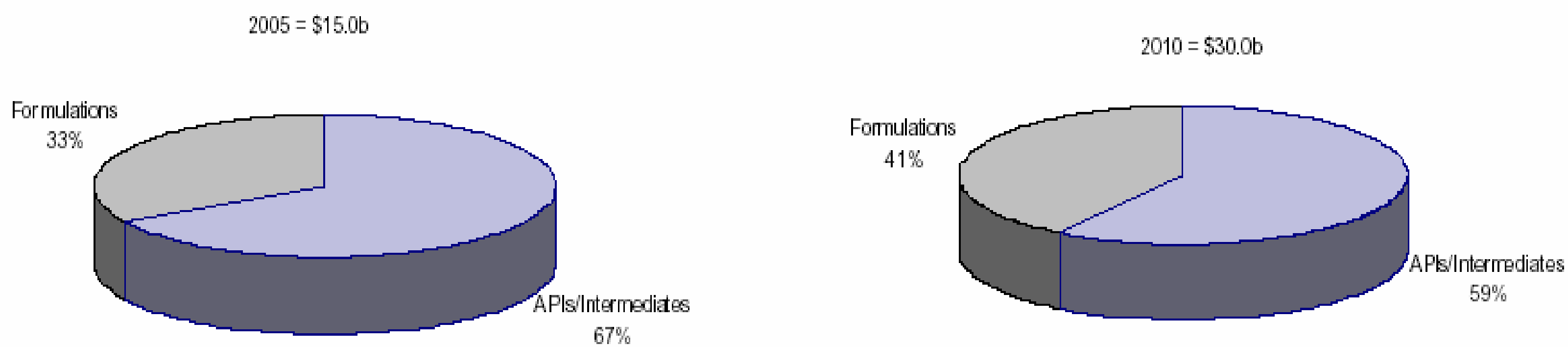
Source: Industry/Motilal Oswal Securities

CRAMS - India on the threshold of a significant opportunity

GLOBAL OUTSOURCING OPPORTUNITY



GLOBAL CONTRACT MANUFACTURING OPPORTUNITY



Source: Industry/Motilal Oswal Securities

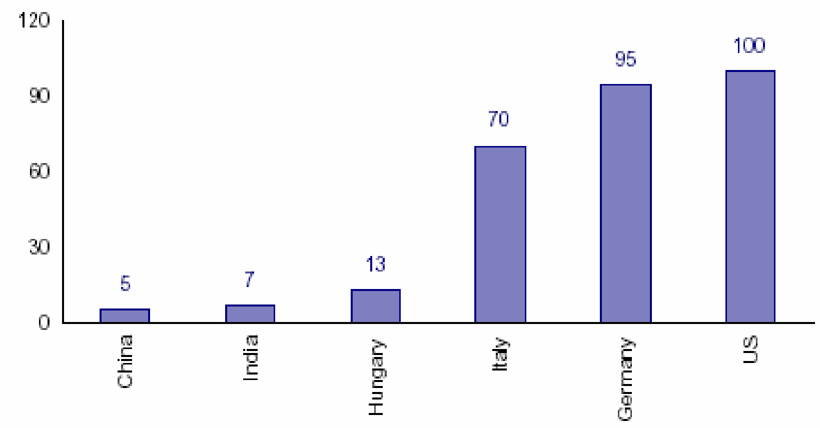
CRAMS - India on the threshold of a significant opportunity

- **The global outsourcing industry is witnessing a gradual shift in business from western nations to low-cost destinations like India, as they are facing tough times due to high cost of operations and large under-utilized capacities.**
- **India has compelling advantages:**
  - **World class quality at 30-40% lower cost**
  - **Proven chemistry and process innovation skills instilled by years of fierce competition in the domestic market**
  - **Established regulatory skills – Highest no. of USFDA approved facilities outside US, accounts for 25-30% of DMF filed**
  - **Patent regime gives comfort to MNCs**
  - **Low labour cost – 1/5th of that of USA**
  - **India has capabilities across CRAMS value chain – from CCS to formulations**

MANUFACTURING COST

COUNTRY	UNITS
US	100
Europe	85-90
India	
US FDA-approved plants	35-40
Others	25-30
China*	20-25

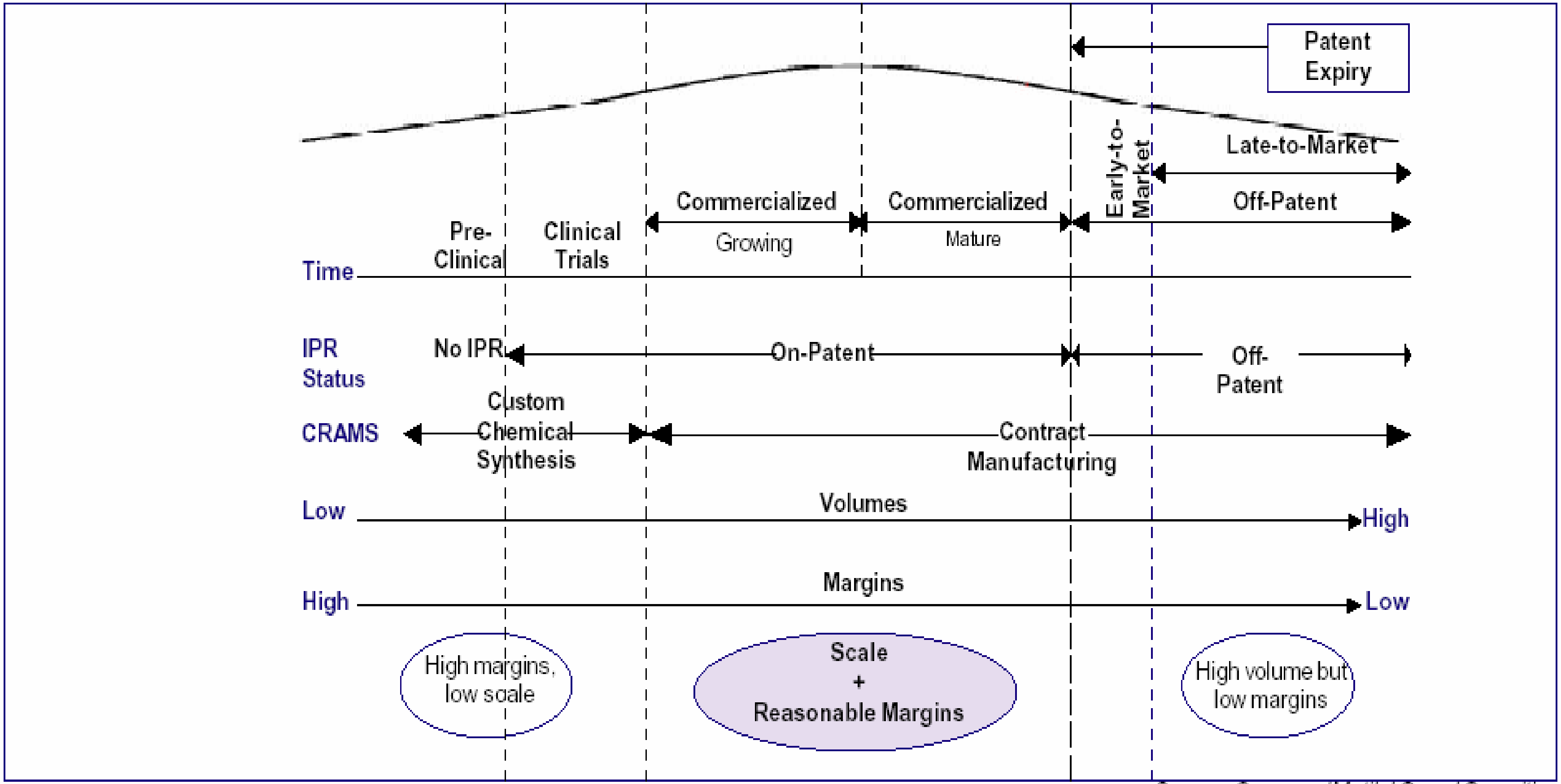
SKILLED CHEMIST COSTS



* China reportedly has few USFDA approved plants; Source: CRISINFAC

Contract manufacturing - the most scalable opportunity

CRAMS VALUE CHAIN

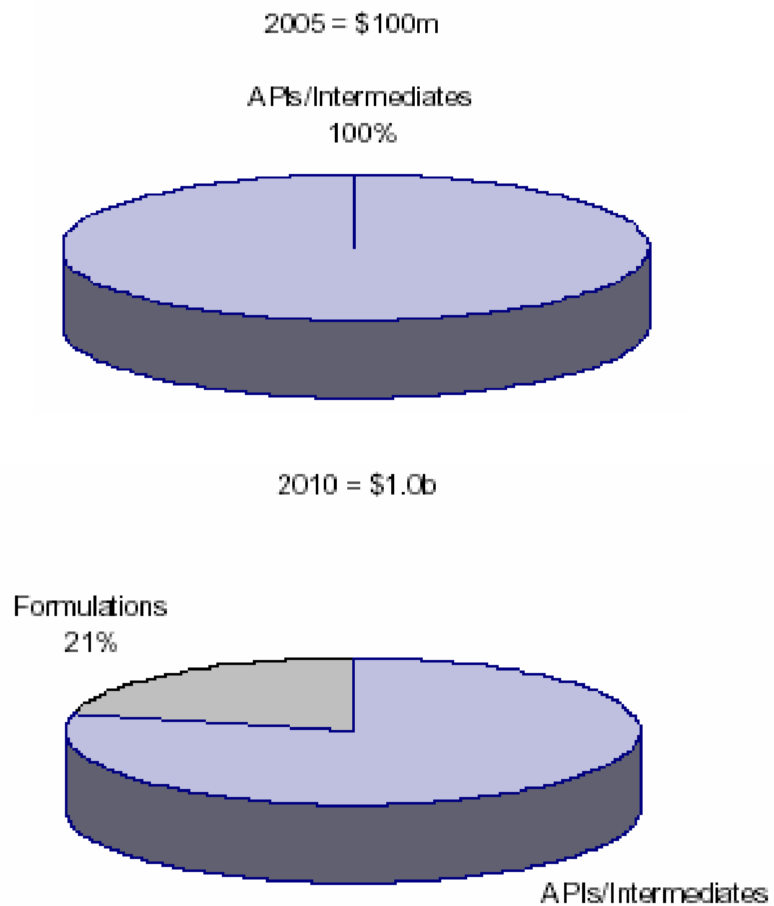


Source: Company/Motilal Oswal Securities

India - Contract manufacturing opportunity

- **Contract manufacturing – the most scalable opportunity for Indian players**
- **CCS would typically involve supply of material at gram or kilogram level, while contract manufacturing involves supplies in tons**
- **CCS supplies are linked to the success of the partner's R&D pipeline and are, hence, volatile**
- **Contract manufacturing supplies, on the other hand, are linked to the success of a product post commercialization**
- **CCS skills important as it gives an opportunity to lock-in into MNC relationship from the development stage itself**

INDIA'S CONTRACT MANUFACTURING OPPORTUNITY



Source: Industry/Motilal Oswal Securities

Very few Indian players set to exploit the opportunity

- **High entry barriers – Top 5 players would get disproportionate share of the $1b opportunity**
  - **Preferred vendors allocated at least 50% of business and hence MNCs are very selective in choosing partners**
  - **Invest significant time and resources to develop MNC relationships**
  - **Reference from existing customers are important**
  - **Strict IPR compliance – most Indian pharma companies are competing against MNCs in the generic segment**
- **Gestation periods would be long**
  - **Indian CRAMS industry is still evolving - potential customers take a long time to award contracts.**
  - **As a test case, the initial offtake by the customer may not be very high.**
  - **Post signing of the contract, it takes 18-24 months for the supplies to begin due to the time-consuming registration process**
  - **Investors should expect a time-gap between signing of contracts and commencement of supplies.**
- **Unlike popular belief, contract manufacturing yields decent margins**
  - **Most of the contract manufacturing deals have been struck at about 20-25% EBITDA margins**
  - **On-patent product supplies are likely to attract higher margins due to the better pricing power enjoyed by the MNC partner**
  - **Given India’s cost advantage and process chemistry skills, 25% EBITDA margins are sustainable for the next few years**

China is not a threat yet

- **It's not just about 'labor arbitrage'**
- **Unique combination of superior chemistry and regulatory skills, as well as good quality at low costs augurs well for India as a preferred outsourcing destination**

CRAMS – INDIA V/S CHINA

PARAMETER	INDIA	CHINA
Manufacturing focus	Advanced Intermediates, APIs, Formulations	Bulk chemicals, Intermediates, Fermentation-based products
Chemistry skills for pharma products	Well developed	Moderately developed
Regulatory skills & compliance	Well established	Weak
Labour costs	Cheap	Less than India
Scientific skills	Good	Moderate
US FDA approved facilities	> 70 - highest outside USA	Very few
DMFs filed	25-30% of global filings	Very few
Product basket offered	Broad	Narrow
MNC Outsourcing stance	Turning favourable	Cautious
MNC confidence for technology transfer	Moderate to High	Weak
MNC relationships	Moderate to High	Weak
IPR Protection	Product patent regime implemented in Jan-05 but still some grey areas	Product patent regime implemented long back but loosely implemented
Domestic pharmaceutical industry	Well developed	Moderately developed
Communication (English language)	Well established	Weak
Infrastructure	Weak	Well developed

Source: Motilal Oswal Securities

Increasing outsourcing to India

- **China is not a threat yet as pharma out-sourcing is not just about 'labor arbitrage', but also about chemistry and regulatory skills as well as good quality**
- **MNCs have commenced outsourcing from India**
- **Most of the products being outsourced are off-patent products**
- **Recently MNCs have shown a willingness to outsource patented products as well**

INDIA – MNC OUTSOURCING TILL DATE

COMPANY	OUTSOURCING FOCUS IN INDIA		
	CLINICAL TRIALS	MANUFACTURING	R&D
GSK	Yes	Yes	Yes
Eli Lilly	Yes	Yes	Yes
Aventis		Yes	
Novartis		Yes	
Abbott		Yes	
Altana		Yes	
Pfizer	Yes		Yes
AstraZeneca		Yes	Yes
Solvay		Yes	
Roche	Yes		

Note: Above information is based on disclosed projects. Details on CCS outsourcing are not available due to confidentiality clauses.

Source: Industry/Motilal Oswal Securities

Companies

Ranbaxy Labs – Buy [RBXY IN; CMP: Rs369; M.Cap:US$3B]

- **Aggressive inorganic initiatives – to gain scale**
  - **Acquired Terapia (Romania) for $324m, 4.1x sales and 11.6x EV/EBITDA**
  - **Terapia enjoys high EBITDA margins of about 35% and NPM of 25%**
  - **It has a pipeline of 60 new authorizations likely to be commercialized over the next 3 years**
  - **Fully integrated player with manufacturing facilities and in-house R&D and clinical trials capabilities**
  - **Ethimed and Allen acquisitions are not very significant for the short-to-medium term**

(Rs m)	**CY05**	**CY06E**	**CY07E**
Ranbaxy Sales	50,974	56,701	64,593
Incremental sales from Terapia acquisition	0	2,141	4,925
Incremental sales from Allen (Italy) acquisition	0	261	435
Incremental sales from Ethimed acquisition	0	335	513
Total Sales	**50,974**	**59,438**	**70,466**
% Growth		*16.6%*	*18.6%*
Ranbaxy core EPS (Rs)	5.8	11.0	13.5
Incremental EPS from Terapia acquisition	0.0	1.3	3.0
Incremental EPS from Allen (Italy) acquisition	0.0	0.1	0.1
Incremental EPS from Ethimed acquisition	0.0	0.1	0.1
Total EPS (Rs)	**5.8**	**12.4**	**16.7**

Ranbaxy Labs – Buy [RBXY IN; CMP: Rs369; M.Cap:US$3B]

- **Looking at more acquisitions – to reach $2b revenue target by CY07E**
  - **Current operations and announced acquisitions - $1.58b sales in CY07E**
  - **Target acquisition with $400m sales**
- **Strong product pipeline for generic markets**
  - **Has 59 ANDAs pending approval, 18 FTFs – one of the strongest pipelines**
  - **Planning to launch 7 FTFs in CY06-07 (~innovator sales of $2.3b) - not factored in our estimates**
  - **Expect at least 10 new launches (excluding FTFs) every year**
- **Statin launches may be delayed – upside not included in estimates**
  - **Company missed the Pravastatin patent expiry deadline (21st Apr) due to 483's – May limit upside**
  - **US FDA has appealed lower court ruling for Simvastatin – Potential one-time upside of Rs6-7/share**
- **Aggressive Capex – Anticipating strong product flow over next few years**
  - **Capex of about $150m in CY05. Planning further capex of $200m over CY06-07**
- **Potential NCE & NDDS R&D hive-off - open to partnerships but a decision not yet taken**
  - **Can result in incremental EPS of Rs2-2.5 – not included in our estimates**
- **Worst is over, expect improvement in coming years despite pricing pressure**
  - **Expect improvement in coming years despite pricing pressure; Future growth to be led by new launches and acquisitions**
  - **Cost cutting, lower litigation expenses will expand EBITDA margins (albeit on lower base)**
  - **Valuations at 29.6x CY06E and 21.9x CY07E earnings (excl. one-time upsides). Maintain Buy**

Ranbaxy Labs – Financials

INCOME STATEMENT					(Rs Million)
Y/E DECEMBER	**2003**	**2004**	**2005**	**2006E**	**2007E**
Net Sales	**44,553**	**52,351**	**50,974**	**56,701**	**64,593**
Net Sales (incl acqn)*	*44,553*	*52,351*	*50,974*	*59,438*	*70,466*
Change (%)	*23.0*	*17.5*	*-2.6*	*16.6*	*18.6*
Other Operating Income	3,447	1,870	1,796	1,806	1,540
Total Expenditure	37,404	44,407	49,659	50,835	56,970
EBITDA	**10,596**	**9,814**	**3,111**	**7,673**	**9,162**
Margin (%)	*22.1*	*18.1*	*5.9*	*13.1*	*13.9*
Depreciation	1,211	1,215	1,445	1,713	1,992
Int. and Finance Charges	252	335	671	917	879
Other Income - Rec.	662	1,000	616	335	347
PBT & EO Expense	**9,795**	**9,264**	**1,612**	**5,378**	**6,639**
Change (%)	*31.3*	*-5.4*	*-82.6*	*233.7*	*23.4*
Extra Ordinary Expense	-352	372	-333	0	0
PBT after EO Exp.	**10,147**	**8,892**	**1,945**	**5,378**	**6,639**
Tax	2,538	1,881	-698	968	1,195
Tax Rate (%)	*25.0*	*21.2*	*-35.9*	*18.0*	*18.0*
Reported PAT	**7,609**	**7,011**	**2,642**	**4,410**	**5,444**
Minority Interest	15	26	26	20	40
Addn due to acquisition*	0	0	0	595	1,326
Adj PAT after Minority	**7,331**	**7,279**	**2,164**	**4,985**	**6,730**
Change (%)	*26.6*	*-0.7*	*-70.3*	*130.3*	*35.0*
Margin (%)	*16.5*	*13.9*	*4.2*	*8.8*	*10.4*

BALANCE SHEET					(Rs Million)
Y/E DECEMBER	**2003**	**2004**	**2005**	**2006E**	**2007E**
Equity Share Capital	1,855	1,859	1,862	1,862	1,862
Fully Diluted Eq Cap	*1,855*	*1,859*	*1,862*	*1,998*	*1,998*
Reserves	19,617	23,140	22,503	24,718	27,460
Revaluation Reserves	110	107	105	105	105
Net Worth	**21,582**	**25,106**	**24,470**	**26,685**	**29,427**
Minority Interest	166	180	166	146	106
Loans	5,850	8,527	20,043	29,461	27,961
Deferred liabilities	943	1072	-49	-49	-49
Capital Employed	**28,541**	**34,885**	**44,629**	**56,243**	**57,445**
Gross Block	16,533	23,132	29,920	32,032	33,532
Less: Accum. Deprn.	6,496	7,838	9,329	11,041	13,033
Net Fixed Assets	**10,037**	**15,294**	**20,591**	**20,991**	**20,499**
Capital WIP	1,005	2,876	5,595	1,000	750
Investments	168	184	172	172	172
Curr. Assets	**31,239**	**34,921**	**33,279**	**54,766**	**58,766**
Inventory	9,558	14,351	13,624	14,603	16,635
Account Receivables	7,511	11,357	11,404	12,314	14,014
Cash and Bank Balance	1,580	1,339	2,430	18,812	17,822
Others	12,590	7,874	5,821	9,038	10,295
Curr. Liability & Prov.	**13,909**	**18,389**	**15,008**	**20,685**	**22,742**
Account Payables	7,791	12,144	10,600	11,185	12,742
Provisions	6,118	6,245	4,408	9,500	10,000
Net Current Assets	**17,330**	**16,532**	**18,271**	**34,081**	**36,024**
Appl. of Funds	**28,541**	**34,885**	**44,629**	**56,243**	**57,445**

*E: MOSt Estimates; * includes Allen, Ethimed and Terapia*

Ranbaxy Labs – Financials

RATIOS					
Y/E DECEMBER	2003	2004	2005	2006E	2007E
Basic (Rs)					
EPS (Fully diluted)*	**19.8**	**19.6**	**5.8**	**12.5**	**16.8**
Cash EPS	23.0	22.8	9.7	16.8	21.8
BV/Share	57.9	67.2	65.4	71.4	78.7
DPS	8.5	8.5	8.5	5.2	6.4
Payout (%)	46.8	51.4	136.8	49.8	49.6
Valuation (x)					
P/E (Fully diluted)		18.8	63.5	29.6	21.9
PEG (x)		-26.6	-0.9	0.2	0.6
Cash P/E		16.2	38.1	22.0	16.9
P/BV		5.5	5.6	5.2	4.7
EV/Sales		2.7	2.9	2.5	2.2
EV/EBITDA		14.7	49.7	19.2	16.1
Dividend Yield (%)		2.3	2.3	1.4	1.7
Return Ratios (%)					
RoE	34.1	29.1	8.9	18.8	23.0
RoCE	35.2	27.5	5.1	11.2	13.1
Working Capital Ratios					
Asset Turnover (x)	1.6	1.5	1.1	1.0	1.1
Debtor (Days)	62	79	82	79	79
Inventory (Days)	78	100	98	94	94
Working Capital (Days)	129	106	113	98	103
Leverage Ratio (x)					
Current Ratio	2.2	1.9	2.2	2.6	2.6
Debt/Equity	0.3	0.3	0.8	1.1	1.0

CASH FLOW STATEMENT					(Rs Million)
Y/E DECEMBER	2003	2004	2005	2006E	2007E
Op. Profit/(Loss) before Tax	10,596	9,814	3,111	7,673	9,162
Interest/Dividends Recd.	662	1,000	616	335	347
Direct Taxes Paid	-2,436	-1,752	-423	-968	-1,195
(Inc)/Dec in WC	-4,675	558	-648	572	-2,933
CF from Operations	**4,147**	**9,620**	**2,656**	**7,611**	**5,381**
EO Expense	-67	372	-333	0	0
CF from Oper. incl EO	**4,214**	**9,248**	**2,989**	**7,611**	**5,381**
(Inc)/Dec in FA	-2,387	-8,342	-9,462	2,484	-1,250
(Pur)/Sale of Investments	202	-16	12	0	0
CF from Investments	**-2,185**	**-8,358**	**-9,450**	**2,484**	**-1,250**
Issue of Shares	0	116	336	0	0
(Inc)/Dec in Debt	1,871	2,691	11,501	9,399	-1,540
Interest Paid	-252	-335	-671	-917	-879
Dividend Paid	-3,561	-3,603	-3,614	-2,195	-2,702
CF from Fin. Activity	**-1,942**	**-1,130**	**7,552**	**6,287**	**-5,121**
Inc/Dec of Cash	**86**	**-240**	**1,091**	**16,382**	**-990**
Add: Beginning Balance	1,494	1,580	1,339	2,430	18,812
Closing Balance	**1,580**	**1,339**	**2,430**	**18,812**	**17,822**

Cipla – Buy [CIPLA IN; CMP:Rs210; M.Cap:US$3.6b]

- **One of the strongest generic pipelines with about 160 products in various stages of development**
- **Unique low-risk partnership model with global generic players (in US & EU)**
  - **Helps in spreading risk associated with generics markets**
  - **Also attempted to spread risks across product categories like plain vanilla generics, patent challenges and FTFs**
- **Pace of product filings by Cipla's partners with the US-FDA is picking up, as our estimate put their filings at 80-90 ANDAs till March'06**
- **Some of these generic product filings could result in significant upsides for Cipla**
  - **Generic Sertraline – Ivax, which has Para-IV FTF for Sertraline, has partnered with Cipla. Supplies have commenced from 1QFY07 and would add around Rs0.3 to Cipla's EPS**
  - **Fulticasone – Ivax, Cipla's partner, has a pending ANDA for Fulticasone. If approved, Fulticasone supplies could add US$30m to Cipla's revenue and Rs0.4 to EPS**
  - **Finasteride - Ivax's Finasteride exclusivity could benefit Cipla, assuming that Cipla partnership with Ivax covers Finasteride. Finasteride could add Rs0.4 to Cipla's EPS**
  - **Seretide – Generic Seretide would throw up multiple opportunities, subject to the successful outcome of patent challenge by Cipla's partner. Upside not included in our estimates**
  - **Tamiflu – Cipla is keen to secure licenses from Roche to make generic versions of Tamiflu, but Roche is yet to grant sub-license to Cipla. However, the Tamiflu opportunity could just be a one-off upside.**

Cipla – Buy [CIPLA IN; CMP:Rs210; M.Cap:US$3.6B]

- **Anti-AIDS products represent a high-volume opportunity, with limited competition**
  - **Cipla is one of the leading players in the anti-AIDS market and is likely to participate in the US government's PEPFAR program for supplying ARVs to under-developed nations**
  - **Expects to register its own ARV drugs with the US-FDA over the next 12-month for PEPFAR program**
  - **Although Cipla is late in getting its product registered with the USFDA, its JV Cipla Medpro is one of the leading generic companies in South Africa**
- **CFC-free inhalers represents good long term potential (EU market size = US$2.6b)**
  - **EU regulations are aimed at encouraging CFC-free inhalers, opening up a large market**
  - **Cipla could also benefit significantly out of its expertise in developing CFC-free inhalers**
  - **However, patent infringement issues cannot be ruled out**
- **The management is undertaking significant capex of Rs8b during FY05-08 to upgrade and expand facilities, implying strong product flow in the coming years**
- **Revenues and earnings to grow at CAGR of 21% and 20% during FY06-08 respectively**
  - **Our estimates include potential upsides from ANDA approvals, but doesn't include upsides from patent challenges filed by Cipla's partners**
- **Valuations at 22.5xFY07E and 18.8xFY08E do not fully reflect the potential upsides from one of the strongest generic pipelines coupled with de-risked strategy**

Cipla – Financials

INCOME STATEMENT					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006**	**2007E**	**2008E**
Net Income	**19,230**	**22,545**	**29,857**	**36,696**	**43,540**
Change (%)	*31.7*	*17.2*	*32.4*	*22.9*	*18.6*
Total Expenditure	15,038	17,592	23,193	27,553	32,498
EBITDA	**4,192**	**4,953**	**6,664**	**9,143**	**11,042**
Margin (%)	*21.8*	*22.0*	*22.3*	*24.9*	*25.4*
Depreciation	403	551	830	951	1,105
Int. and Finance Charges	104	76	114	96	84
Other Income - Rec.	356	817	1,311	360	270
PBT before EO Items	**4,041**	**5,143**	**7,031**	**8,455**	**10,122**
Extra Ordinary Expense	207	0	0	0	0
Profit before Taxes but	**3,833**	**5,143**	**7,031**	**8,455**	**10,122**
Tax	878	1,050	1,030	1,184	1,417
Tax Rate (%)	*19.0*	*20.4*	*14.6*	*14.0*	*14.0*
Reported PAT	**2,956**	**4,093**	**6,001**	**7,272**	**8,705**
Adj PAT	**3,274**	**4,093**	**6,001**	**7,272**	**8,705**
Change (%)	*32.2*	*25.0*	*46.6*	*21.2*	*19.7*
Margin (%)	*17.0*	*18.2*	*20.1*	*19.8*	*20.0*

BALANCE SHEET					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006**	**2007E**	**2008E**
Equity Share Capital	600	600	600	1,555	1,555
Reserves	11,939	14,835	19,468	31,831	38,764
Revaluation Reserves	102	102	102	102	102
Net Worth	**12,641**	**15,536**	**20,169**	**33,487**	**40,420**
Loans	2,106	1,950	2,200	1,302	1,502
Deferred liabilities	659	889	792	707	606
Capital Employed	**15,406**	**18,376**	**23,161**	**35,497**	**42,528**
Gross Block	7,408	9,867	11,967	13,067	16,367
Less: Accum. Deprn.	1,932	2,478	3,308	4,259	5,364
Net Fixed Assets	**5,476**	**7,389**	**8,660**	**8,808**	**11,003**
Capital WIP	560	1,060	960	450	500
Investments	1,804	183	1,266	1,266	1,266
Curr. Assets	**14,362**	**17,529**	**21,677**	**36,041**	**42,452**
Inventory	5,689	7,457	9,141	11,270	13,397
Account Receivables	4,982	5,873	6,207	7,658	9,121
Cash and Bank Balance	62	154	1,667	11,562	13,285
Others	3,628	4,045	4,661	5,551	6,649
Curr. Liability & Prov.	**6,796**	**7,785**	**9,401**	**11,068**	**12,692**
Account Payables	6,796	7,785	9,401	11,068	12,692
Net Current Assets	**7,566**	**9,744**	**12,276**	**24,973**	**29,759**
Appl. of Funds	**15,406**	**18,376**	**23,161**	**35,497**	**42,528**

E: MOSt Estimates

Cipla – Financials

RATIOS					
Y/E MARCH	2004	2005	2006	2007E	2008E
Basic (Rs)					
EPS	**4.4**	**5.5**	**8.0**	**9.4**	**11.2**
Cash EPS	4.9	6.2	9.1	10.6	12.6
BV/Share	16.7	20.6	26.8	43.0	51.9
DPS	1.2	1.4	1.6	1.8	2.0
Payout (%)	34.3	29.2	22.8	21.9	20.4
Valuation (x)					
P/E		38.5	26.2	22.4	18.8
Cash P/E		33.9	23.0	19.9	16.6
P/BV		10.2	7.8	4.9	4.0
EV/Sales		7.3	5.5	4.2	3.5
EV/EBITDA		33.3	24.6	16.7	13.7
Dividend Yield (%)		0.7	0.8	0.9	1.0
Return Ratios (%)					
RoE	26.1	26.5	29.9	21.8	21.6
RoCE	26.9	28.4	30.8	24.1	24.0
Working Capital Ratios					
Asset Turnover (x)	1.2	1.2	1.3	1.0	1.0
Debtor (Days)	95	95	76	76	76
Inventory (Days)	108	121	112	112	112
Working Capital (Days)	144	158	150	248	249
Leverage Ratio (x)					
Current Ratio	2.1	2.3	2.3	3.3	3.3
Debt/Equity	0.2	0.1	0.1	0.0	0.0

CASH FLOW STATEMENT					(Rs Million)
Y/E MARCH	2004	2005	2006	2007E	2008E
Oper. Profit/(Loss) before Ta	4,192	4,953	6,664	9,143	11,042
Interest/Dividends Recd.	356	817	1,311	360	270
Direct Taxes Paid	-780	-820	-1,128	-1,268	-1,518
(Inc)/Dec in WC	-690	-2,086	-1,019	-2,802	-3,064
CF from Operations	**3,077**	**2,863**	**5,829**	**5,433**	**6,730**
(inc)/dec in FA	-2,440	-2,964	-2,000	-590	-3,350
(Pur)/Sale of Investments	-538	1,621	-1,083	0	0
CF from Investments	**-2,977**	**-1,343**	**-3,083**	**-590**	**-3,350**
(Inc)/Dec in Debt	1,158	-155	250	-898	200
Interest Paid	-104	-76	-114	-96	-84
Dividend Paid	-1,015	-1,197	-1,368	-1,595	-1,773
CF from Fin. Activity	**39**	**-1,429**	**-1,232**	**5,052**	**-1,657**
Inc/Dec of Cash	**-69**	**92**	**1,513**	**9,895**	**1,723**
Add: Beginning Balance	131	62	154	1,667	11,562
Closing Balance	**62**	**154**	**1,667**	**11,562**	**13,285**

Dr. Reddy's Labs – Buy [DRRD IN; CMP: Rs1,271; M.Cap:US$2.1B]

- **Betapharm – Extended payback but gives strategic entry to Germany**
  - **Recently acquired for $576m (3x sales), 11.7x EV/EBITDA**
  - **4th largest player in Germany with 3.5% share and a sales force of 250 people**
  - **Plans to launch 20 new products over the next few years**
  - **Recent price cuts to extend payback**
  - **Expect sales to grow by 10% to Rs9.6b and PAT to decline by 12% to Rs1.1b for CY06E**
- **US Generics – Significant opportunities in next 12 months**
  - **Expect US business to grow by 28% and 51% for FY07E and FY08E respectively led by new launches (Incremental sales of $10m and $28m) excluding one-time opportunities**
  - **One-time opportunities - Incremental EPS of Rs34 & Rs12 for FY07E and FY08E respectively.**

(US$ M)	FY07E	FY08E	FY08E (sustainable)
Sales			
- Generic Allegra	27.96	7.00	7.00
- Generic Zofran	22.50	25.31	2.8
- Generic Zocor	106.88	11.25	11.25
- Generic Proscar	8.79	0.88	0.88
Total Sales	**166.12**	**44.44**	**21.94**
Incremental EPS (Rs)			
- Generic Allegra	8.24	1.22	1.22
- Generic Zofran	9.12	9.53	0.41
- Generic Zocor	15.31	1.30	1.30
- Generic Proscar	1.26	0.10	0.10
Total EPS (Rs)	**33.93**	**12.15**	**3.03**

Dr. Reddy's Labs – Buy [DRRD IN; CMP: Rs1,271; M.Cap:US$2.1B]

- **Plavix patent settlement could result in significant upsides**
  - **Plavix commands revenues of about $3.0b in the US. Sanofi has already settled with Apotex (FTF)**
  - **Sanofi has indicated settlement with DRL also**
  - **Settlement could result in upside of $100m over the next 5-6 years**
- **Other businesses growing at a steady pace**
  - **Branded formulation exports to record CAGR of 25% till FY08E**
  - **API exports to record CAGR of 20% till FY08E**
  - **Custom pharmaceutical services to reach $100m sales by FY08E mainly led by the Mexico acquisition**
- **GPM to improve to 51.5% by FY08E compared to the current 48.8%**
- **DRL has taken significant steps to revitalize its business with a focus on reducing risks and gaining scale.**
- **It has also taken a more balanced approach for its US product portfolio to reduce reliance on Para-IVs**
- **Betapharm acquisition has strengthened presence in Europe**
- **DRL is currently valued at 20.9x FY07E and 19.9x FY08E earnings (excluding one-time upsides)**
- **We reiterate Buy rating.**

Dr. Reddy's Labs – Financials

INCOME STATEMENT					(Rs Million)
Y/E MARCH	2004	2005	2006E	2007E	2008E
Net Sales	**20,081**	**19,183**	**24,266**	**38,577**	**44,462**
Change (%)	*11.1*	*-4.5*	*26.5*	*59.0*	*15.3*
Total Expenditure	17,516	18,722	22,599	34,294	38,299
Operating Income	**2,565**	**461**	**1,667**	**4,283**	**6,163**
Change (%)	*-30.8*	*-82.0*	*261.4*	*156.9*	*43.9*
Margin (%)	*12.8*	*2.4*	*6.9*	*11.1*	*13.9*
Amortization	382	350	420	690	600
EBIT	**2,183**	**111**	**1,247**	**3,593**	**5,563**
Other Income - Rec. (incl Fo	828	-15	252	-270	-270
PBT & EO Expense	**3,011**	**96**	**1,499**	**3,323**	**5,293**
Change (%)	*-21.0*	*-96.8*	*1,458.2*	*121.7*	*59.3*
Extra Ordinary Expense	385	-11	-388	0	0
PBT after EO Expense	**2,626**	**107**	**1,887**	**3,323**	**5,293**
Tax	69	-94	258	365	635
Tax Rate (%)	*2.6*	*-88.0*	*13.7*	*11.0*	*12.0*
Minority Interest	-3	-10	0	0	0
Reported PAT	**2,560**	**211**	**1,629**	**2,957**	**4,658**
PAT adj for EO Items	**2,932**	**190**	**1,371**	**2,957**	**4,658**
Adjusted Net Profit	**2,932**	**190**	**1,371**	**2,957**	**4,658**
Change (%)	*-14.0*	*-93.5*	*621.0*	*115.6*	*57.5*
Margin (%)	*14.6*	*1.0*	*5.7*	*7.7*	*10.5*

BALANCE SHEET (EXCL BETAPHARM)					(Rs Million)
Y/E MARCH	2004	2005	2006E	2007E	2008E
Equity Share Capital	383	383	383	383	383
Reserves	20,657	20,571	21,559	23,751	27,835
Net Worth	**21,039**	**20,953**	**21,942**	**24,134**	**28,218**
Loans	628	2,945	9,132	9,132	9,132
Deferred Liabilities/Tax	708	373	197	104	55
Capital Employed	**22,375**	**24,272**	**31,271**	**33,370**	**37,405**
Net Fixed Assets	**6,421**	**7,160**	**9,386**	**13,066**	**13,986**
Investments	4,379	1,487	1,105	1,105	1,105
Goodwill/Intangible Assets	2,666	2,588	10,042	10,042	10,042
Curr. Assets	**13,002**	**17,816**	**17,411**	**19,765**	**24,499**
Inventory	3,032	3,500	6,895	5,787	6,669
Account Receivables	3,774	3,609	4,802	7,137	8,225
Cash and Bank Balance	4,483	9,346	3,712	3,659	5,936
Others	1,713	1,362	2,002	3,183	3,668
Curr. Liability & Prov.	**4,092**	**4,780**	**6,673**	**10,609**	**12,227**
Account Payables	2,375	1,555	6,067	9,644	11,115
Other Current Liabilities	1,717	3,225	607	964	1,112
Net Current Assets	**8,909**	**13,036**	**10,738**	**9,157**	**12,272**
Appl. of Funds	**22,375**	**24,272**	**31,271**	**33,370**	**37,405**

*E: MOSt Estimates *As per US GAAP*

Dr. Reddy's Labs – Financials

RATIOS					
Y/E MARCH	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Basic (Rs)					
EPS	**38.3**	**2.5**	**17.9**	**38.6**	**60.9**
Cash EPS	43.3	7.1	23.4	47.7	68.7
BV/Share	275.0	273.8	286.8	315.4	368.8
DPS	5.0	5.0	5.0	10.0	7.5
Payout (%)	14.4	222.3	30.8	28.6	13.6
Valuation (x)					
P/E		511.3	70.9	32.9	20.9
PEG (x)		-5.5	0.1	0.3	0.4
Cash P/E		180.0	54.3	26.7	18.5
P/BV		4.6	4.4	4.0	3.4
EV/Sales		4.7	4.2	2.6	2.2
EV/EBITDA		193.8	60.9	23.7	16.1
Dividend Yield (%)		0.4	0.4	0.8	0.6
Return Ratios (%)					
RoE	13.9	0.9	6.2	12.3	16.5
RoCE	13.5	0.4	4.8	10.0	14.2
Working Capital Ratios					
Asset Turnover (x)	0.9	0.8	0.8	1.2	1.2
Debtor (Days)	69	69	72	68	68
Inventory (Days)	55	67	104	55	55
Working Capital (Days)	80	70	106	52	52
Leverage Ratio					
Current Ratio (x)	3.2	3.7	2.6	1.9	2.0
Debt/Equity (x)	0.0	0.1	0.4	0.4	0.3

CASH FLOW STATEMENT (EXCL BETAPHARM)					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Oper. Profit/(Loss) before Ta	2,565	461	1,667	4,283	6,163
Interest/Dividends Recd.	828	-15	252	-270	-270
Direct Taxes Paid	-69	94	-258	-365	-635
(Inc)/Dec in WC	131	735	-3,335	1,529	-839
CF from Operations	**3,455**	**1,275**	**-1,674**	**5,176**	**4,419**
EO Expense	385	-11	-388	0	0
CF from Operating incl	**3,070**	**1,286**	**-1,286**	**5,176**	**4,419**
(inc)/dec in FA	-2,416	-1,089	-2,646	-4,370	-1,520
(Pur)/Sale of Investments	-4,156	2,892	382	0	0
CF from Investments	**-6,572**	**1,803**	**-2,264**	**-4,370**	**-1,520**
Issue of Shares	5	0	0	0	0
(Inc)/Dec in Debt	460	2,318	6,187	0	0
Other Items	652	-111	-7,848	-435	223
Dividend Paid	-432	-423	-423	-423	-846
CF from Fin. Activity	**686**	**1,784**	**-2,084**	**-858**	**-623**
Inc/Dec of Cash	**-2,816**	**4,862**	**-5,634**	**-52**	**2,277**
Add: Beginning Balance	7,300	4,483	9,346	3,712	3,659
Closing Balance	**4,484**	**9,346**	**3,712**	**3,660**	**5,936**

GlaxoSmithKline Pharma – Buy **[GLXO IN; CMP:Rs1,008; M.Cap:US$1.9B]**

- **One of the best plays on IPR regime in India as GSK has aggressive initiatives for the Indian market**
  - **Planning to launch 8 patented products by CY09, including 4 new vaccines (see table below)**
  - **Expects patented products to contribute about 50% of its revenues by 2015**
  - **Access to strong R&D pipeline of parent, with about 117 new products in various stages of clinical trials**
- **CY06-07 will witness change in product-mix with increasing contribution of the life-style segment**
  - **Planning to enter the high-growth segments of CNS, CVS and Diabetology**
  - **Expects to launch 3-5 new products annually for the next two years**
  - **Open to in-licensing good brands from other pharmaceutical companies to bridge the gaps in its proposed life-style portfolio**
- **Will have to share margins on patented products with the parent**

GSK PLC. – R&D PIPELINE

PHASE	NO. OF DRUGS
Pre-clinical	N.A.
Phase I	48
Phase II	46
Phase III	23
Total	117

Source: GSK Plc.

PRODUCT	THERAPEUTIC SEGMENT	LAUNCH YEAR
Rotarix	Rotavirus Vaccine	2007
Cervarix	Cervical cancer Vaccine	2007/08
Infanrix	Infant Vaccine	2007/08
Lapatinib	Cancer	2008
Allermist	Respiratory	2008
Alvimopan	Post-operative Ileus	2008
Pleuromutilin		2008
Streptorix	Pneumonia Vaccine	2009

Source: Company

GlaxoSmithKline Pharma – Buy **[GLXO IN; CMP:Rs1,008; M.Cap:US$1.9B]**

- **Strong vaccine portfolio**
  - **GSK's new vaccine sales have grown by about 27% CAGR, constituting about 93% of total vaccine sales**
  - **Plans to launch four patented vaccines in the Indian market in the CY07-09 period**
- **New launches have started contributing meaningfully to revenues**
  - **New introductions (launches post 2001) contributed about Rs1b to GSK's CY05 revenue**
  - **Growth has been led mainly by aggressive new launches as well as improvement in MR productivity**
- **DPCO coverage has reduced from 40% to 29% in last five years**
- **Our earnings estimates for CY07E factor in:**
  - **Additional marketing and promotional expenditure linked to launch of patented products in CY07E**
  - **Impact of the divestment of the animal healthcare unit**
- **Valuations at 22.2xCY06E and 21.7xCY07E do not fully reflect:**
  - **The strong parentage (giving access to a large product pipeline)**
  - **Brand-building ability and it's likely positioning in the post patent era**
  - **The potential upside from product patents would create 'option value' in longer term**
  - **Key risks – Government proposal to reduce drug prices could have an adverse impact**

GlaxoSmithKline Pharma– Financials

INCOME STATEMENT					(Rs Million)
Y/E DECEMBER	**2003^**	**2004**	**2005E**	**2006E**	**2007E**
Exports	340	284	255	230	207
Net Domestic Sales	10,592	13,351	14,448	16,532	16,944
Net Sales	**10,932**	**13,635**	**14,704**	**16,762**	**17,151**
Change (%)	*4.4*	*24.7*	*7.8*	*14.0*	*2.3*
Total Expenditure	8,443	9,780	10,424	11,535	11,969
EBITDA	**2,489**	**3,855**	**4,280**	**5,227**	**5,182**
Change (%)	*43.0*	*54.9*	*11.0*	*22.1*	*-0.9*
Margin (%)	*22.8*	*28.3*	*29.1*	*31.2*	*30.2*
Depreciation	179	175	157	193	202
Int. and Finance Charges	26	25	0	18	15
Other Income - Rec.	563	528	656	771	961
PBT & EO Expense	**2,846**	**4,182**	**4,779**	**5,788**	**5,926**
Tax	1,027	1,522	1,716	1,945	1,991
Tax Rate (%)	*36.1*	*36.4*	*35.9*	*33.6*	*33.6*
Adj PAT	**1,819**	**2,660**	**3,063**	**3,843**	**3,935**
EO Expense (net of tax)	96	-670	-1,258	-1,324	0
Reported PAT	**1,722**	**3,331**	**4,321**	**5,167**	**3,935**
Change (%)	*41.6*	*46.3*	*15.1*	*25.5*	*2.4*
Margin (%)	*15.8*	*24.4*	*29.4*	*30.8*	*22.9*

E: MOSt Estimates ^ - Standalone results

BALANCE SHEET					(Rs Million)
Y/E DECEMBER	**2003^**	**2004**	**2005E**	**2006E**	**2007E**
Equity Share Capital	745	873	847	847	847
Reserves	5,914	8,353	7,911	10,180	12,570
Capital Reserve	17	17	17	17	17
Net Worth	**6,675**	**9,243**	**8,775**	**11,044**	**13,433**
Loans	29	38	28	28	28
Capital Employed	**6,703**	**9,281**	**8,803**	**11,072**	**13,461**
Gross Block	2,567	2,526	2,626	2,826	3,026
Less: Accum. Deprn.	1,614	1,657	1,814	2,007	2,209
Net Fixed Assets	**953**	**870**	**813**	**820**	**818**
Capital WIP	41	45	40	40	40
Investments	4,091	7,768	6,729	8,978	11,456
Curr. Assets	**4,346**	**4,846**	**4,999**	**5,699**	**5,831**
Inventory	2,009	2,265	2,353	2,682	2,744
Account Receivables	671	761	809	922	943
Cash and Bank Balance	594	634	662	754	772
Others	1,072	1,187	1,176	1,341	1,372
Curr. Liability & Prov.	**3,028**	**4,697**	**4,117**	**4,693**	**4,802**
Account Payables	2,061	2,195	2,500	2,850	2,916
Other Liabilities					
Provisions	967	2,502	1,617	1,844	1,887
Net Current Assets	**1,318**	**149**	**882**	**1,006**	**1,029**
Deferred Tax Assets	300	449	339	229	119
Appl. of Funds	**6,703**	**9,281**	**8,803**	**11,072**	**13,461**

E: MOSt Estimates ^ - Standalone results

GlaxoSmithKline Pharma– Financials

RATIOS

Y/E DECEMBER	2003^	2004	2005E	2006E	2007E
Basic (Rs)					
EPS	**24.4**	**30.5**	**36.2**	**45.4**	**46.5**
Cash EPS	26.8	32.5	38.0	47.6	48.8
BV/Share	89.6	105.8	103.6	130.4	158.6
DPS	10.0	24.0	15.0	16.0	16.0
Payout (%)	46.2	89.1	88.3	40.2	39.3
Valuation					
P/E	41.3	33.1	27.9	22.2	21.7
Cash P/E	37.6	31.0	26.5	21.2	20.6
P/BV	11.2	9.5	9.7	7.7	6.4
EV/Sales	7.4	5.6	5.3	4.5	4.3
EV/EBITDA	32.4	20.0	18.2	14.5	14.1
Dividend Yield (%)	1.0	2.4	1.5	1.6	1.6
Return Ratios (%)					
RoE	27.2	28.8	34.9	34.8	29.3
RoCE	42.8	45.3	54.3	52.4	44.1
Working Capital Ratios					
Asset Turnover (x)	1.6	1.5	1.7	1.5	1.3
Debtor (Days)	22	20	20	20	20
Inventory (Days)	67	61	58	58	58
Working Capital (Days)	24	-13	5	5	5
Leverage Ratio					
Debt/Equity	0.0	0.0	0.0	0.0	0.0

E: MOSt Estimates ^ - Standalone results

CASH FLOW STATEMENT

Y/E DECEMBER	2003^	2004	2005E	2006E	2007E
Oper. Profit/(Loss) before Ta	2,434	3,855	4,280	5,227	5,182
Interest/Dividends Recd.	563	528	656	771	961
Direct Taxes Paid	-935	-1,670	-1,606	-1,835	-1,881
(Inc)/Dec in WC	-66	-321	-1,040	1,128	-6
CF from Operations	**1,996**	**2,391**	**2,290**	**5,292**	**4,256**
EO expense	164	-670	-1,258	-1,324	0
CF from Operating incl	**1,832**	**3,062**	**3,548**	**6,616**	**4,256**
(inc)/dec in FA	76	36	-95	-200	-200
(Pur)/Sale of Investments	-2,119	-3,677	1,039	-2,249	-2,478
CF from investments	**-2,043**	**-3,641**	**944**	**-2,449**	**-2,678**
Issue of Shares	0	1,606	-2,084	-29	0
(Inc)/Dec in Debt	9	10	-10	0	0
Interest Paid	-19	-25	0	-18	-15
Dividend Paid	-590	-840	-2,370	-2,704	-1,545
CF from Fin. Activity	**-600**	**751**	**-4,464**	**-2,751**	**-1,560**
Inc/Dec of Cash	**-811**	**171**	**28**	**1,416**	**17**
Add: Beginning Balance@	1,406	594	634	662	754
Closing Balance	**595**	**765**	**662**	**2,078**	**772**

E: MOSt Estimates ^ - Standalone results

Divis Labs – Buy [DIVI IN; CMP: Rs1,204; M.Cap:US$337M]

- **Generic business – to grow at a steady pace**
  - **Older generic products (FY05 sales-43%) enjoy strong positioning as it is among top-3 globally**
  - **Filed 8 DMFs during FY06, taking total to 26 DMFs; Expects to file another 6-7 in FY07E**
  - **While its older products are expected to grow at steady pace, initial contribution from new generic products would add to the growth FY08 onwards**

- **CCS business to expand in coming years**
  - **Currently working with 20 of the top-25 global innovator companies as it enjoys good reputation with them and has been able to effectively demonstrate its chemistry skills**
  - **Commands the largest CCS pipeline from India consisting of about 55 products, of which 25 are in Phase-III trials**

- **Setting up new facility under SEZ scheme**
  - **Divis is setting up a new facility at Vizag, at a capex of Rs800m, under SEZ scheme for which it would enjoy fiscal benefits – To be commissioned gradually beginning 4QFY07**
  - **We believe that the company has some existing contracts on hand which will be serviced out of this new SEZ.**
  - **Our estimates do not include upsides from this SEZ**

Divis Labs – Buy [DIVI IN; CMP: Rs1,204; M.Cap:US$337M]

- **Peptides and nucleotides offer good growth potential**
  - **Already developed chemical synthesis capabilities for key intermediates and building blocks for peptides, which have been approved by several users. It has commercialized some of these products and can now offer key starting materials or synthesized intermediates**
  - **Developing nucleotide building blocks and is in the early stage of developing the process for four major protected nucleotides.**
  - **Both peptides & nucleotides involve complex chemistry and hold immense long-term potential**

- **Carotenoids: supplies to commence shortly**
  - **Global carotenoids market, including food, feed and pharma, is estimated at US$1b**
  - **Initially, we expect Divis to participate in the incremental growth (~15% p.a) market for Astaxanthin (market size-US$300)**
  - **Supplies to commence by 2QFY07**

- **P&G Contract has been shelved – Expect one-time write off**
- **Divis is expected to record an earnings CAGR of 16% till FY08, led by reasonable top-line growth (12-13% CAGR) and a gradual 210bp margin expansion. The company is currently valuated at 19.5x FY07E and 14.7x FY08E earnings. Our estimates, however, do not include upsides from any future contracts that the company may announce or from the Rs800m SEZ facility. We reiterate Buy rating.**

Divis Labs – Financials

INCOME STATEMENT					(Rs Million)
Y/E MARCH	2004	2005	2006E	2007E	2008E
Net Sales	**3,028**	**3,474**	**3,779**	**4,337**	**4,928**
Change (%)	*22.8*	*14.7*	*8.8*	*14.8*	*13.6*
Total Expenditure	1,987	2,428	2,595	3,013	3,339
% of Sales	*65.6*	*69.9*	*68.7*	*69.5*	*67.8*
EBITDA	**1,041**	**1,046**	**1,185**	**1,324**	**1,589**
Margin (%)	*34.4*	*30.1*	*31.3*	*30.5*	*32.2*
Depreciation	132	151	149	236	275
EBIT	**909**	**895**	**1,035**	**1,088**	**1,314**
Int. and Finance Charges	34	43	73	140	122
Other Income - Rec.	145	171	103	183	207
PBT before EO Expense	1,020	1,024	1,065	1,131	1,399
Extra Ordinary Expense/(Income)		0	0	0	0
PBT after EO Expense	1,020	1,024	1,065	1,131	1,399
Current Tax	243	330	320	249	280
Deferred Tax	45	27	32	90	73
Tax Rate (%)	*28.2*	*34.9*	*33.0*	*30.0*	*25.2*
Reported PAT	**728**	**661**	**714**	**792**	**1,046**
PAT Adj for EO Items	**732**	**666**	**714**	**792**	**1,046**
Change (%)	*33.2*	*-9.0*	*7.1*	*10.9*	*32.2*
Margin (%)	*24.2*	*19.2*	*18.9*	*18.3*	*21.2*

BALANCE SHEET					(Rs Million)
Y/E MARCH	2004	2005	2006E	2007E	2008E
Equity Share Capital	128	128	128	128	128
Total Reserves	2,164	2,708	3,290	3,964	4,854
Net Worth	**2,292**	**2,837**	**3,419**	**4,092**	**4,982**
Deferred liabilities	223	250	282	373	445
Total Loans	659	661	1,653	1,708	1,297
Capital Employed	**3,174**	**3,748**	**5,354**	**6,173**	**6,724**
Gross Block	2,236	2,538	3,138	4,138	4,438
Less: Accum. Deprn.	573	723	872	1,108	1,384
Net Fixed Assets	**1,663**	**1,815**	**2,266**	**3,030**	**3,055**
Capital WIP	55	11	63	83	89
Investments	1	0	750	320	500
Curr. Assets	**2,115**	**2,717**	**3,119**	**3,664**	**4,153**
Inventory	1,076	1,390	1,512	1,735	1,971
Account Receivables	867	1,022	1,247	1,431	1,626
Cash and Bank Balance	72	45	77	172	185
Loans & Advances	100	260	283	325	370
Curr. Liability & Prov.	**660**	**795**	**844**	**924**	**1,072**
Account Payables	532	678	680	781	887
Provisions	128	117	164	143	184
Net Current Assets	**1,455**	**1,922**	**2,275**	**2,740**	**3,081**
Appl. of Funds	**3,174**	**3,748**	**5,354**	**6,173**	**6,724**

E: MOSt Estimates

Divis Labs – Financials

RATIOS					
Y/E MARCH	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Basic (Rs)					
EPS	**28.5**	**52.0**	**55.7**	**61.8**	**81.6**
Cash EPS	33.7	63.7	67.3	80.2	103.1
BV/Share	89.4	221.3	266.7	319.2	388.6
DPS	8.0	8.0	10.3	9.2	12.2
Payout (%)	15.9	17.7	18.5	15.0	15.0
Valuation (x)					
P/E		23.2	21.6	19.5	14.7
Cash P/E		18.9	17.9	15.0	11.7
P/BV		5.4	4.5	3.8	3.1
EV/Sales		4.6	4.5	3.9	3.4
EV/EBITDA		15.3	14.4	12.8	10.4
Dividend Yield (%)		0.7	0.9	0.8	1.0
Return Ratios (%)					
RoE	36.9	26.0	22.8	21.1	23.1
RoCE	41.6	33.1	26.6	23.4	25.2
Working Capital Ratios					
Debtor (Days)	103	106	113	113	113
Creditor (Days)	154	156	148	151	156
Inventory (Days)	130	146	146	146	146
Working Capital Turnover (I	167	197	212	216	214
Leverage Ratio (x)					
Current Ratio	3.2	3.4	3.7	4.0	3.9
Debt/Equity	0.3	0.2	0.5	0.4	0.3

CASH FLOW STATEMENT					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Oper. Profit/(Loss) before T	1,041	1,046	1,185	1,324	1,589
Interest/Dividends Recd.	145	171	103	183	207
Direct Taxes Paid	-243	-330	-320	-249	-280
(Inc)/Dec in WC	-648	-493	-322	-369	-328
CF from Operations	**295**	**394**	**646**	**889**	**1,188**
EO Expense / (Income)	0	0	0	0	0
CF from Operating inc	**295**	**394**	**646**	**889**	**1,188**
(inc)/dec in FA	-340	-259	-652	-1,020	-306
(Pur)/Sale of Investments	0	1	-750	430	-180
CF from Investments	**-364**	**-263**	**-1,402**	**-590**	**-486**
Issue of Shares	0	1	0	0	0
(Inc)/Dec in Debt	225	2	992	55	-411
Interest Paid	-34	-43	-73	-140	-122
Dividend Paid	-116	-117	-132	-118	-156
Others	20	0	0	0	0
CF from Fin. Activity	**96**	**-158**	**788**	**-203**	**-689**
Inc/Dec of Cash	**27**	**-27**	**32**	**95**	**13**
Add: Beginning Balance	45	72	45	77	172
Closing Balance	**72**	**45**	**77**	**172**	**185**

Matrix Laboratories – Buy [HDPH IN; CMP: Rs225; M.Cap:US$755M]

- **Inorganic growth strategy**
  - **Expand manufacturing capacity, with access to US-FDA approved facilities**
  - **Expand product portfolio**
  - **Gain access to technologies/capabilities currently not available in-house**
  - **Backward & forward integration**
  - **Access to front-end of the market**

MATRIX: INORGANIC STRATEGY

COMPANY	COUNTRY	SEGMENT	ACQUISITION COST	MATRIX STAKE (%)	REMARK
DocPharma	Belgium	Generics	US$238m	100	Strengthens presence in European generics market
FCC	South Africa	Generics	US$20m	50	Strengthens generics product basket with 25 non-overlaping DMF filings
Sigma Labs	India	Generics	Not disclosed	100	Forward integration into manufacture of formulations. May be utilized for manufacturing products for DocPharma
Concord Biotech	India	Generics	Not disclosed	55	Gains access to biotech and fermentation based products as well as a USFDA approved biotech facility
Explora Labs	Switzerland	Generics/ CRAMS	Not disclosed	43	Gain access to technology platforms for oncology and high potency products. Also gains contacts with innovator companies for the CRAMS business
Astrix	India	ARV	Matrix transferred assets, technology & IP for ARVs for US$36m	50	Benefits from Aspen's dominance in ARVs and gets assured volume
MCHEM	China	ARV	US$15-20m	60	Backward integration into intermediates would ehance cost-effectiveness

Source: Company/Motilal Oswal Securities

Matrix Laboratories – Buy [HDPH IN; CMP: Rs225; M.Cap:US$755M]

- **Anti-retrovirals (ARVs) – a sustainable volume play**
  - **ARV opportunity driven by western funding and a relaxation in IPR regulations**
  - **Matrix has tie-ups with three of the largest players (Aspen, Cipla & Ranbaxy)**
  - **Unlike popular belief, margins for ARVs are reasonable**
  - **Expect 36% sales CAGR to Rs5.5b by FY08**
- **Generic business gathering momentum**
  - **Strong pipeline of about 90 DMFs by end-FY07 (only 10 commercialized till date)**
  - **Expects 10 new launches in FY07E**
  - **Strong chemistry skills – Non-infringing process (Citalopram and one patent settlement)**
- **European operations**
  - **Acquisition of DocPharma gives it access to the European generics market with part-synergies of backward integration expected from FY07 onwards.**
  - **Expects 8 new launches in FY07E – initially planned in FY06**
  - **Planning to divest medical devices business of DocPharma (sales of Rs2.14b in FY06)**
  - **Unlikely to dilute equity for $100m loan repayment**
- **A larger generic product basket and entry into more stable areas such as ARVs lends greater stability to its revenues and profitability. To become partner-of-choice for API sourcing from India. At 18.9x FY07E and 15.1x FY08E consolidated earnings, we maintain Buy.**

Matrix Laboratories – Financials

INCOME STATEMENT (CONSOLIDATED)					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006**	**2007E**	**2008E**
Net Sales	**5,295**	**6,368**	**11,586**	**16,442**	**18,440**
Change (%)	*33.9*	*20.3*	*82.0*	*41.9*	*12.2*
Total Expenditure	3,628	4,660	10,270	14,035	15,533
EBITDA	**1,667**	**1,708**	**1,316**	**2,407**	**2,907**
Margin (%)	*31.5*	*26.8*	*11.4*	*14.6*	*15.8*
Depreciation	111	191	335	391	414
EBIT	**1,556**	**1,517**	**981**	**2,015**	**2,493**
Int. and Finance Charges	179	63	269	520	432
Other Income - Rec.	103	68	916	720	721
PBT before EO Expense	1,479	1,522	1,629	2,215	2,782
Extra Ordinary Exp./(Inc)	0	0	-753	0	0
PBT after EO Exp	1,479	1,522	2,382	2,215	2,782
Current Tax	117	408	376	177	223
Deferred Tax	116	-100	0	155	195
Tax Rate (%)	*15.8*	*20.2*	*15.8*	*15.0*	*15.0*
Minority Int/Share of loss	0	0	-14	-53	-79
Reported PAT	**1,246**	**1,215**	**1,992**	**1,830**	**2,286**
Adj PAT	**1,246**	**1,215**	**1,358**	**1,830**	**2,286**
Change (%)	*66.0*	*-2.5*	*11.8*	*34.8*	*24.9*
Margin (%)	*23.5*	*19.1*	*11.7*	*11.1*	*12.4*

BALANCE SHEET (CONSOLIDATED)					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Equity Share Capital	127	299	307	307	307
Total Reserves	1,655	5,941	9,211	10,831	12,841
Net Worth	**1,782**	**6,240**	**9,518**	**11,138**	**13,148**
Minority Interest	0	0	1,634	1,672	1,721
Deferred liabilities	276	175	363	518	713
Total Loans	2,075	461	11,250	7,200	7,200
Capital Employed	**4,132**	**6,876**	**22,765**	**20,528**	**22,782**
Gross Block	3,091	4,323	8,648	9,648	9,898
Less: Accum. Deprn.	837	999	2,162	2,553	2,967
Net Fixed Assets	**2,254**	**3,324**	**6,486**	**7,095**	**6,931**
Capital WIP	416	388	500	250	150
Goodwill	0	0	8,790	8,790	8,790
Investments	31	1,595	1,595	31	1,431
Curr. Assets	**2,816**	**4,426**	**10,574**	**11,405**	**13,186**
Inventory	1,251	1,710	3,765	4,439	5,348
Account Receivables	942	1,367	3,650	4,357	4,887
Cash and Bank Balance	36	88	842	307	370
Loans & Advances	587	1,261	2,317	2,302	2,582
Curr. Liability & Prov.	**1,384**	**2,856**	**5,180**	**7,043**	**7,706**
Account Payables	1,084	2,046	3,360	4,933	5,071
Provisions	300	810	1,820	2,111	2,635
Net Current Assets	**1,432**	**1,570**	**5,394**	**4,362**	**5,480**
Appl. of Funds	**4,132**	**6,876**	**22,765**	**20,528**	**22,782**

E: MOSt Estimates

Matrix Laboratories – Financials

RATIOS (CONSOLIDATED)					
Y/E MARCH	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Basic (Rs)					
EPS	**9.8**	**8.1**	**8.8**	**11.9**	**14.9**
Cash EPS	10.7	9.4	15.1	14.5	17.6
BV/Share	14.0	41.7	62.0	72.5	85.6
DPS	0.2	1.2	1.2	1.5	2.0
Payout (%)	13.7	16.9	10.5	14.4	15.5
Valuation (x)					
P/E		27.7	25.5	18.9	15.1
Cash P/E		24.0	14.9	15.6	12.8
P/BV		5.4	3.6	3.1	2.6
EV/Sales		5.5	3.9	2.5	2.2
EV/EBITDA		20.5	34.2	17.2	14.2
Dividend Yield (%)		0.5	0.5	0.7	0.9
Return Ratios (%)					
RoE	89.1	30.3	25.3	17.7	18.8
RoCE	53.7	30.0	13.8	14.0	16.6
Working Capital Ratios					
Debtor (Days)	65	78	115	97	97
Creditor (Days)	172	236	181	192	180
Inventory (Days)	86	98	119	99	106
Working Capital Turnover (I	96	85	143	90	101
Leverage Ratio (x)					
Current Ratio	2.0	1.5	2.0	1.6	1.7
Debt/Equity	1.2	0.1	1.4	0.8	0.6

CASH FLOW STATEMENT (CONSOLIDATED)					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006E**	**2007E**	**2008E**
Oper. Profit/(Loss) before T	1,667	1,708	1,316	2,407	2,907
Interest/Dividends Recd.	103	68	916	720	721
Direct Taxes Paid	-117	-408	-188	-177	-223
(Inc)/Dec in WC	-565	-87	-3,070	497	-1,055
CF from Operations	**1,087**	**1,281**	**-1,025**	**3,446**	**2,350**
EO Expense / (Income)	0	0	-753	0	0
CF from Operating inc	**1,087**	**1,281**	**-272**	**3,446**	**2,350**
(inc)/dec in FA	-1,270	-1,232	-3,610	-750	-150
(Pur)/Sale of Investments	3	-1,564	0	1,564	-1,400
CF from Investments	**-1,267**	**-2,796**	**-3,610**	**814**	**-1,550**
Issue of Shares	-309	3,448	1,482	0	0
Inc/(Dec) in Debt	768	-1,614	10,789	-4,050	0
Interest Paid	-179	-63	-269	-520	-432
Dividend Paid	-171	-205	-210	-264	-355
Others	20	0	-7,157	38	49
CF from Fin. Activity	**129**	**1,566**	**4,636**	**-4,795**	**-737**
Inc/Dec of Cash	**-51**	**52**	**754**	**-535**	**63**
Add: Beginning Balance	87	36	88	842	307
Closing Balance	**36**	**88**	**842**	**307**	**370**

E: MOSt Estimates

Nicholas Piramal – Buy [NP IN; CMP: Rs177; M.Cap:US$807M]

- **CRAMS business gaining traction**
  - **Already announced six contract till date and two international acquisitions in the CRAMS space**
  - **Expects to announce more contracts, including a large formulations contract, in next 12mths**
  - **Has recently acquired Pfizer's UK unit with committed sales of $350m spread over next 5-6 years.**
  - **CRAMS pipeline is expected to have peak sales of US$170-200m (including announced contracts and acquisitions)**

- **Avecia acquisition - a significant step forward**
  - **It strengthens CRAMS pipeline (~93 CCS & Manufacturing contracts), add new clients (~55 existing clients), gives access to critical technologies (like fermentation, biotransformation, chiral synthesis & high potency substance) and access to process R&D team including 53 PhDs**
  - **Although Avecia will turn earnings accretive only FY08, it will bring in long-term benefits**

- **Pfizer acquisition - makes it the largest contract manufacturer for Pfizer**
  - **Committed revenues of $350m from Pfizer till Nov-2011 (majority is front-ended)**
  - **Incremental EPS of Rs1.23 and Rs1.97 for FY07E and FY08E – not included in our estimates**
  - **UK operations (including Avecia & Pfizer's unit) to be EPS accretive in FY07E despite Avecia's losses**

Nicholas Piramal – Buy **[NP IN; CMP: Rs177; M.Cap:US$807M]**

- **Domestic business – expect improvement after a bad FY06**
  - **MRP-based excise, VAT and Phensedyl controversy impacted FY06 sales**
  - **Commissioning of facilities in excise-exempt zone will mitigate impact of MRP-based excise**
  - **Phensedyl sales recovering with current annualized run-rate of Rs1.2b compared to peak annual sales of Rs1.45b in FY05.**
  - **Company expects to out-perform average industry growth**
- **CRAMS has long gestation periods – 18 to 24 months post announcement of contracts**
- **Company has relationships with many large MNC pharmaceutical companies – Pfizer, AstraZeneca, Novartis**
- **IPR compliance – does not challenge MNC patents**
- **At 19.9x FY07E and 15.4x FY08E EPS (excluding Pfizer UK unit acquisition), investors need to take a long-term view on NPIL since the major benefits of the CRAMS business will be visible only by FY08E. Given the expected traction in the CRAMS business, we maintain Buy.**

Nicholas Piramal – Financials

INCOME STATEMENT					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006**	**2007E**	**2008E**
Net Sales	**13,915**	**13,082**	**15,825**	**19,628**	**22,223**
Change (%)	*18*	*-6.0*	*21.0*	*24.0*	*13.2*
Total Expenditure	11,107	11,388	13,840	16,551	18,460
EBITDA	**2,809**	**1,694**	**1,986**	**3,076**	**3,763**
Margin (%)	*20.2*	*12.9*	*12.5*	*15.7*	*16.9*
Depreciation	529	524	688	962	1,006
Int. and Finance Charges	238	276	173	246	314
Other Income - Rec.	257	419	392	271	298
PBT before EO Expense	**2,299**	**1,312**	**1,517**	**2,139**	**2,742**
EO Expense/(Income)	-256	-796	33	0	0
PBT after EO Expense	**2,555**	**2,108**	**1,484**	**2,139**	**2,742**
Tax	41	465	210	278	329
Tax Rate (%)	*16*	*22.0*	*14.1*	*13.0*	*12.0*
Reported PAT	**2,515**	**1,643**	**1,275**	**1,861**	**2,413**
PAT Adj for EO Items	**2,263**	**1,023**	**1,303**	**1,861**	**2,413**
Change (%)	*32.9*	*-54.8*	*27.4*	*42.8*	*29.7*
Margin (%)	*16.3*	*7.8*	*8.2*	*9.5*	*10.9*
Less: Mionrity Interest & Othe	6	3	4	5	10
Adj Net Profit	**2,257**	**1,020**	**1,299**	**1,856**	**2,403**

BALANCE SHEET					(Rs Million)
Y/E MARCH	**2004**	**2005**	**2006**	**2007E**	**2008E**
Equity Share Capital	380	380	418	418	418
Preference Share Capital	534	534	534	0	0
Reserves	3,668	4,620	9,907	9,062	10,035
Net Worth	**4,582**	**5,533**	**10,859**	**9,480**	**10,453**
Minority Interest	41	41	30	35	45
Deferred Liabilities	379	596	836	950	1,070
Total Loans	3,573	3,680	3,114	3,924	3,924
Capital Employed	**8,575**	**9,850**	**14,839**	**14,390**	**15,492**
Gross Block	6,637	8,026	12,657	13,357	14,357
Less: Accum. Deprn.	1,392	1,799	2,488	3,450	4,456
Net Fixed Assets	**5,245**	**6,227**	**10,169**	**9,907**	**9,901**
Capital WIP	432	1,052	249	190	433
Investments	52	37	287	287	287
Curr. Assets	**5,594**	**5,705**	**7,792**	**8,868**	**10,689**
Inventory	1,952	2,755	2,812	3,926	4,970
Account Receivables	1,819	1,460	2,429	4,246	5,325
Cash and Bank Balance	254	155	700	-1,040	-1,690
Others	1,569	1,336	1,851	1,737	2,084
Curr. Liability & Prov.	**2,748**	**3,171**	**3,658**	**4,863**	**5,819**
Account Payables	1,948	2,366	2,687	3,667	4,399
Provisions	800	804	971	1,196	1,420
Net Current Assets	**2,846**	**2,535**	**4,134**	**4,006**	**4,870**
Appl. of Funds	**8,575**	**9,850**	**14,839**	**14,390**	**15,491**

E: MOSt Estimates

Nicholas Piramal – Financials

RATIOS

Y/E MARCH	2004	2005	2006	2007E	2008E
Basic (Rs)					
EPS	**11.9**	**5.4**	**6.2**	**8.9**	**11.5**
Cash EPS	14.7	8.1	9.5	13.5	16.3
BV/Share	21.3	26.3	49.4	45.4	50.0
DPS	3.0	3.0	3.0	5.0	6.0
Payout (%)	26.3	41.5	58.6	65.8	59.3
Valuation (x)					
P/E		33.0	28.5	19.9	15.4
Cash P/E		21.8	18.6	13.1	10.9
P/BV		6.7	3.6	3.9	3.5
EV/Sales		3.1	2.5	2.1	1.9
EV/EBITDA		23.9	19.8	13.6	11.3
Dividend Yield (%)		1.7	1.7	2.8	3.4
Return Ratios (%)					
RoE	53.1	22.5	17.0	18.7	24.1
RoCE	26.1	18.3	14.6	17.4	22.0
Working Capital Ratios					
Asset Turnover (x)	1.6	1.3	1.1	1.4	1.4
Debtor (Days)	48	41	56	79	87
Inventory (Days)	51	77	65	73	82
Working Capital (Days)	75	71	95	74	80
Leverage Ratio (x)					
Current Ratio	2.0	1.8	2.1	1.8	1.8
Debt/Equity	0.9	0.7	0.3	0.4	0.4

CASH FLOW STATEMENT **(Rs Million)**

Y/E MARCH	2004	2005	2006	2007E	2008E
Oper. Profit/(Loss) before Ta:	3,047	1,694	1,986	3,076	3,763
Interest/Dividends Recd.	186	419	392	271	298
Direct Taxes Paid	-90	-248	30	-164	-210
(Inc)/Dec in WC	-196	213	-1,054	-1,612	-1,514
CF from Operations	**2,947**	**2,078**	**1,354**	**1,572**	**2,337**
EO Expense/(income)	256	-796	33	0	0
CF from Oper. incl EO E	**2,691**	**2,874**	**1,321**	**1,572**	**2,337**
(Inc)/Dec in FA	-652	-2,126	-3,828	-641	-1,243
(Pur)/Sale of Investments	-689	15	-250	0	0
CF from Investments	**-1,341**	**-2,112**	**-4,078**	**-641**	**-1,243**
Issue of Shares	-100	-9	4,787	-2,010	0
Inc/(Dec) in Debt	-332	107	-566	810	0
Interest Paid	-469	-276	-173	-246	-314
Dividend Paid	-456	-682	-747	-1,224	-1,430
CF from Fin. Activity	**-1,357**	**-861**	**3,301**	**-2,670**	**-1,744**
Inc/Dec of Cash	**-5**	**-99**	**545**	**-1,740**	**-650**
Add: Beginning Balance	240	254	155	700	-1,040
Closing Balance	**254**	**155**	**700**	**-1,040**	**-1,690**

MOSt Pharma Universe: Comparative Valuations

		CMP (Rs)	Sales (Rs m)	*Sales gr (%)*	OPM (%)	Net profit (Rs m)	EPS (Rs)	*EPS gr (%)*	PE (x)	EV/EBITDA (x)	EV/Sales (X)	RoE (%)	RoCE (%)	Target price (Rs)
Cipla	2006A	210	29,857	*32.4*	22.3	6,001	8.0	*46.6*	26.3	9.5	2.1	29.9	30.8	
	2007E		36,696	*22.9*	24.9	7,272	9.4	*21.2*	22.5	16.8	4.2	21.8	24.1	
	2008E		43,540	*18.6*	25.4	8,705	11.2	*19.7*	18.8	13.7	3.5	21.6	24.0	280
Dr Reddy's	2006A	1,271	24,266	*26.5*	6.9	1,371	17.9	*621.0*	70.9	60.9	4.2	6.2	4.8	
	2007E		38,577	*59.0*	11.1	2,957	38.6	*115.6*	32.9	23.7	2.6	12.3	10.0	
	2008E		44,462	*15.3*	13.9	4,658	60.9	*57.5*	20.9	16.1	2.2	16.5	14.2	1,600
	2008E*		45,449	*17.8*		4,893	63.9		19.9					
Ranbaxy (Y/E Dec)	2005A	369	50,974	*-2.6*	6.1	2,164	5.8	*-70.3*	63.6	49.9	3.0	8.9	5.1	
	2006E		56,701	*16.6*	13.5	4,985	12.5	*130.3*	29.6	19.3	2.6	18.8	11.2	
	2007E		64,593	*18.6*	14.2	6,730	16.8	*35.0*	21.9	13.1	1.9	23.0	13.1	565
Aventis (Y/E Dec)	2005A	1,505	8,022	*9.8*	28.4	1,591	69.1	*10.5*	21.8	13.9	4.0	31.9	46.7	
	2006E		9,010	*12.3*	28.5	1,805	78.4	*13.4*	19.2	11.8	3.4	29.1	41.8	2,100
	2007E		9,974	*10.7*	28.1	1,978	85.9	*9.6*	17.5	10.3	2.9	26.3	38.0	
Glaxo +BW (Y/E Dec)	2005A	1,008	14,704	*7.8*	29.1	3,063	36.2	*15.1*	27.9	18.2	5.3	34.9	54.3	
	2006E		16,762	*14.0*	31.2	3,843	45.4	*25.5*	22.2	14.5	4.5	34.8	52.4	1,394
	2007E		17,151	*2.3*	30.2	3,935	46.5	*2.4*	21.7	14.1	4.3	29.3	44.1	
Pfizer (Y/E Nov)	2005A	776	6,161	*5.8*	21.5	827	27.7	*44.5*	28.0	15.9	3.4	22.0	36.1	
	2006E		7,017	*13.9*	23.6	1,074	36.0	*29.9*	21.6	12.8	3.0	24.9	39.4	1,000
	2007E		7,789	*11.0*	24.7	1,260	42.2	*17.2*	18.4	10.6	2.6	25.5	39.7	
Divis Labs	2006E	1,204	3,779	8.8	31.3	714	56	*7.1*	21.6	14.4	4.5	22.8	26.6	
	2007E		4,337	14.8	30.5	792	62	*10.9*	19.5	12.8	3.9	21.1	23.4	1764
	2008E		4,928	13.6	32.2	1,046	82	*32.2*	14.7	10.4	3.4	23.1	25.2	
Lupin	2006A	943	16,954	*35.0*	13.2	1,730	39	*88.0*	24.1	20.8	2.7	30.9	20.6	
	2007E		20,066	*18.4*	15.1	2,537	57	*46.3*	16.4	14.7	2.2	34.8	21.3	975
	2008E		22,557	*12.4*	16.2	3,118	71	*22.9*	13.4	11.9	1.9	33.0	23.9	
Matrix Labs	2006E	225	11,586	*82.0*	11.4	1,358	8.8	*8.98*	25.5	34.2	3.9	25.3	13.8	
	2007E		16,442	*41.9*	14.6	1,830	11.9	*34.77*	18.9	17.2	2.5	17.7	14.0	290
	2008E		18,440	*12.2*	15.8	2,286	14.9	*24.89*	15.1	14.2	2.2	18.8	16.6	
NPIL	2006A	177	15,825	*21.0*	12.5	1,299	6	*27.4*	28.5	19.7	2.5	17.0	14.6	
	2007E		19,628	*24.0*	15.7	1,856	9	*42.8*	19.9	13.5	2.1	18.7	17.4	315
	2008E		22,223	*13.2*	16.9	2,403	11	*29.7*	15.4	11.2	1.9	24.1	22.0	
Sun Pharma	2006E	736	15,931	39.3	31.2	5,732	28	43.0	26.6	26.9	8.4	42.0	19.9	
	2007E		18,891	18.6	31.5	6,545	32	13.1	23.3	22.1	7.0	37.7	20.8	800
	2008E		22,731	20.3	33.5	7,899	38	21.2	19.3	16.6	5.6	35.9	22.2	
Wockhardt (Y/E Dec)	2005A	351	13,660	12	20.7	2,110	18	19	19.8	15.5	3.2	29.5	16.0	
	2006E		16,296	19	23.9	2,943	25	39	14.2	12.1	2.9	32.5	21.5	536
	2007E		18,819	15	25.1	3,662	31	24	11.4	9.2	2.3	32.3	25.7	

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