



Dishman Pharma

STOCK INFO.	BLOOMBERG
BSE Sensex: 19,243	DISH IN
	REUTERS CODE
S&P CNX: 5,702	DISH.BO

26 October 2007

Buy

Previous Recommendation: Buy

Rs295

Equity Shares (m)	81.6
52-Week Range	350/188
1,6,12 Rel. Perf. (%)	-12/3/10
M.Cap. (Rs b)	24.0
M.Cap. (US\$ b)	0.6

YEAR	NET SALES	PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END*	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
03/07A	5,750	893	11.0	94.1	26.8	6.7	35.4	15.6	5.1	26.2
03/08E	8,035	1,129	13.9	26.5	21.2	5.1	30.8	15.8	3.7	17.9
03/09E	9,735	1,501	18.5	32.9	16.0	3.9	31.1	16.7	3.0	13.7

Dishman's 2Q results were better than estimates. Key highlights:

- Net sales were up 60% to Rs1.87b, driven by 73% YoY growth in CRAMS revenue (to Rs1.4b) and 29% YoY growth in marketable molecules to Rs463m. While stand-alone CRAMS sales have increased by 30%, consolidation of Carbogen-AMCIS (CA) acquisition has boosted overall CRAMS growth.
- EBITDA margins expanded by 70bp to 21.7%, driven by strong margin expansion at Carbogen AMCIS (23% margins excluding forex gains) and improvement in business mix in favor of CRAMS (75.2% of sales vs 69.5% in 2QFY07). Impact of higher other income (due to forex gain of Rs60m) was negated by higher depreciation (at Rs111m vs Rs41m in 2QFY07) and higher interest cost (at Rs72m vs Rs38m). Higher than estimated tax provisioning at 10.3% of PBT restricted PAT growth to 68% to Rs282m.
- Guidance** - Management has maintained its earlier guidance of 30-35% top-line growth for FY08 (including CA). Carbogen is targeting 15-20% revenue growth for FY08. Management has indicated that some of its contract prices are likely to be increased to counter an appreciating currency and its impact will be visible over the next few quarters.
- Key growth drivers for Dishman will be ramp-up in the India-based contracts, with supplies to Solvay expected to record 25% for CAGR for FY07-09, while non-Solvay contracts are expected to grow at 50% CAGR (albeit on a low base). We believe that Dishman will be a key beneficiary of the increased pharmaceutical outsourcing from India. Based on our current estimates, Dishman is valued at 21.2x FY08E and 16x FY09E consolidated earnings. Maintain **Buy**.

QUARTERLY PERFORMANCE (CONSOLIDATED)

(Rs Million)

Y/E MARCH	FY07				FY08				FY07	FY08E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Net Sales	822	1,170	1,736	2,057	1,680	1,866	2,115	2,374	5,786	8,035
YoY Change (%)	34.7	71.0	180.3	139.1	104.2	59.5	21.8	15.4	108.5	38.9
Total Expenditure	620	924	1,248	1,840	1,406	1,461	1,675	1,823	4,632	6,364
EBITDA	202	246	488	218	274	405	440	551	1,154	1,671
Margins (%)	24.6	21.0	28.1	10.6	16.3	21.7	20.8	23.2	19.9	20.8
Depreciation	34	41	156	31	89	111	110	102	263	412
Interest	9	38	72	44	61	72	73	71	162	277
Other Income	34	42	34	122	107	91	30	32	232	260
PBT after EO Income	193	209	294	265	230	314	287	410	961	1,241
Tax	8	39	43	-77	4	32	23	40	13	99
Deferred Tax	0	2	7	9	12	0	3	-3	19	12
Rate (%)	4.3	19.6	17.1	-25.4	7.0	10.3	9.0	9.2	3.3	9.0
Reported PAT	185	168	244	332	214	282	261	372	929	1,129
YoY Change (%)	96.4	23.4	25.8	634.1	15.7	67.8	6.9	12.1	97.9	21.6
Margins (%)	22.5	14.3	14.1	16.2	12.7	15.1	12.3	15.7	16.1	14.1

E: MOST Estimates

CRAMS business and consolidation of Carbogen-AMCIS drives top-line growth

Net sales were up 60% to Rs1.87b, driven by 73% YoY growth in CRAMS revenue (to Rs1.4b) and 29% YoY change in marketable molecules to Rs463m. While stand-alone CRAMS sales have increased by 30%, consolidation of Carbogen-AMCIS (CA) acquisition has boosted overall CRAMS growth. CA contributed CHF26.24m (~ Rs891m) to overall revenues.

REVENUE BREAK-UP (RS M)

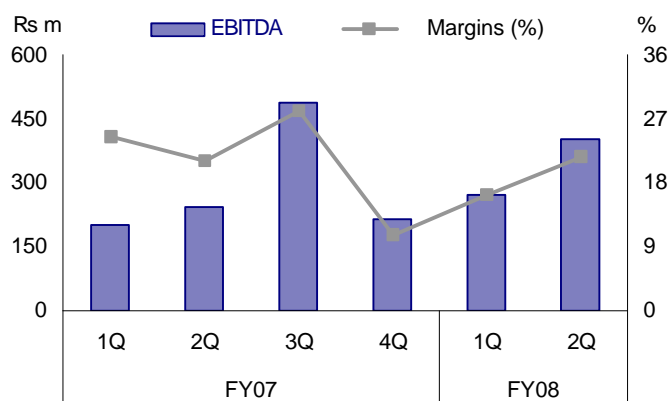
	2Q		YOY	1Q	
	FY08	FY07		FY08	GR (%)
CRAMS	1,403	810	73.1	1,245	12.7
Dishman	512	313	63.4	462	10.8
CA	891	497	79.3	783	13.8
MM	463	360	28.7	435	6.4
Total	1,866	1,170	59.5	1,680	11.1

Source: Company/Motilal Oswal Securities

However, increased costs and one-time write-offs impact EBITDA margins

EBITDA margins expanded by 70bp to 21.7% (vs est. of 19.2%), driven by strong margin expansion at Carbogen AMCIS (CA) at 23% excluding forex gains. Shifting of 8 projects from CA to Dishman's India operations has also had a +ve impact on margins. EBITDA margins have improved despite the currency appreciation and increase in input costs imported from China, due to better margins at CA.

TREND IN EBITDA MARGIN



Source: Company/Motilal Oswal Securities

PAT grew by 68% to Rs282m due to better performance from CA and was partly boosted by forex gains of Rs60m.

Price increases to partly offset currency appreciation in 2HFY08

Dishman has taken selective price increases in its CRAMS business and significant increase for the QUATS business to counter the significant currency appreciation. The impact of these increases is likely to be visible in 2HFY08 and is expected to partly offset the adverse impact on margins resulting in a better performance in 2HFY08 over 1HFY08.

Guides 30%-35% top-line growth for FY08

Management has guided 30-35% top-line growth for FY08 (incl. Carbogen acqn.). Carbogen is targeting 15-20% revenue growth for FY08. Management has also indicated that it is likely to maintain EBITDA margins at FY07 levels (21.4% adjusted for one-time write-offs). While we expect a higher sales growth of about 40% for FY08E, we are forecasting a lower EBITDA margin at 20.8% due to higher RM, staff & SG&A costs and currency appreciation. Management has indicated that some of its contract price are likely to be increased to counter an appreciating currency and their impact will be visible over the next few quarters.

New contract announcements expected in 2HFY08

Dishman management has indicated that it has further strengthened its relationship with Solvay by including more supply agreements and is likely to disclose more details on these new contracts in 2HFY08. While these contracts are likely to contribute to revenues only in the long-term, the announcements regarding such contracts is likely to impart more visibility for Dishman's CRAMS business. We believe that this will be a long-term positive for the long-term.

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

Dishman acquired Carbogen-AMCIS (Switzerland) in Aug-2006 for US\$74.5m (~ 0.7x EV/Sales and 4x EV/EBITDA

based on CY06 financials). The acquisition was funded by a combination of FCCB issue (US\$50m), internal accrual and debt.

CA is a pharmaceutical services provider, offering a broad portfolio of drug development and commercialization services to the pharmaceutical and biopharmaceutical industries at all stages of drug development since 1982. CA has a customer base comprising mid-sized pharmaceutical and biopharmaceutical companies as well as the large MNCs. It enjoys business relationships with 7 of 10 pharmaceutical majors with 75% of its revenues accruing from the USA.

Owing to its strong CRAMS capabilities, CA has been able to retain most of its customers despite the restructuring undertaken by its parent (Solutia). In fact, around 90% of its 2005 revenue was generated from repeat customers. Carbogen's specialty is handling contract research projects, whereas AMCIS has a repertoire of seven APIs under long-term contract manufacturing (at its USFDA and Swiss medic approved facility).

The combined entity has the capability of serving the entire drug life cycle of 15-20 years. Dishman expects to drive synergies with CA by expanding the combined product basket and renewing its focus on key accounts. Dishman will be able to improve CA's profitability by outsourcing development of intermediates to Dishman and leveraging on Dishman's marketing support for Asia Pacific etc. This acquisition has completely transformed the business mix of Dishman by giving Dishman's CRAMS offering a new dimension.

Solvay's EM supplies will get a boost going forward

Dishman is currently a key supplier of Eprosartan Mesylate API (anti-hypertensive) to Solvay, which markets it under the brand, Teveten. Solvay sources this product from two of its key suppliers – Dishman & Lonza. Dishman also supplies some intermediates of Eprosartan Mesylate to Solvay, but in negligible amounts. The Solvay contract is

valid until 2008 and extendable annually thereafter. However, the patent for Eprosartan Mesylate (EM) is valid until 2013.

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

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

Currently Solvay sources about 50% of its EM requirement from Dishman. The latter has expanded its capacity at the Bavla facility from 60 tpa to 200 tpa in order to meet the increased offtake from Solvay. On the back of the potentially higher volume offtake ahead, we expect EM supplies to Solvay to generate about Rs1-1.2b in revenues (up 27% YoY) for Dishman in FY08E. Supplies are expected to stabilize at ~Rs1.5b by FY09E.

Looking beyond Solvay – Other contracts to ramp up in coming years

Currently, Solvay is Dishman's major client contributing close to 18% of Dishman's total sales and about 25% of its CRAMS revenues. To reduce its dependence on a single customer, Dishman has entered into supply arrangements with several other MNCs for both on-patent as well off-patent supplies of APIs and intermediates.

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

DISHMAN – CRAMS RELATIONSHIPS

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

Source: Company

Dependence on Solvay has reduced considerably: The signing of more supply contracts with various multinational companies as well as the CA acquisition has reduced Dishman's dependence on Solvay to a great extent. The latter accounted for about 32% of Dishman's total revenues and 100% of its CRAMS revenues in FY04. This proportion is now expected to come down to about 15% and 18% respectively for FY08E led by signing of new contracts and contribution from CA acquisition. Given the strong relationship with Solvay, we expect the latter's contribution to range between 15-20% of Dishman's total sales in forthcoming years.

Capex/investments of Rs1.1b for FY08

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

PROPOSED ACTIVITY

	CAPEX (RS M)	FUNDING
Expansion of Dishman's facilities in India	500	Internal accruals
Doubling of AMCIS high-potency capacity	320	& debt
Dishman's Chinese & Saudi Arabia initiatives	300	
Total	1,120	

Source: Company

Valuation and recommendation

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

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

We expect Dishman's core revenues (excluding CA acquisition) to grow at 26% CAGR over FY07-FY09. CA is expected to record about 15-18% growth in CY07E and CY08E. Contribution of CRAMS (including CA) is expected to improve from 53% of total revenues in FY06 to about 80% by FY09E, led by scale-up in EM supplies to Solvay, contribution from new contracts and the CA acquisition. Supplies to Solvay are expected to record 21% CAGR over FY07-FY09 while other contracts (excluding CA) are expected to grow at 53% CAGR, albeit on a low base. The Marketable Molecules (MM) division is expected to record a steady 15% CAGR in revenues for this period. We have not assumed any revenues from Dishman's initiatives in China and Saudi Arabia, as we believe that upsides from these measures are still some time away.

Dishman is currently valued at 21.2x FY08E and 16x FY09E consolidated earnings. Given Dishman's capabilities to offer the complete range of CRAMS services (from the pre-clinical stage up to commercialization), we believe that valuations are likely to expand gradually as new CRAMS assignments start contributing to revenues. CRAMS will account for about 80% of consolidated revenues FY08E onward. We maintain **Buy** with price target of Rs330.

Dishman Pharma: an investment profile

Company description

Dishman has become one of the key players in the Indian CRAMS space. It has gradually moved up the value chain from being a pure chemicals supplier to a CRAMS player by virtue of both its organic and inorganic initiatives in this space. The acquisition of Carbogen-AMCIS has enabled the company to offer the complete range of services across the CRAMS value chain.

Key investment arguments

- ✍ Strong supply agreement with Solvay. The company has established relationships with other large innovator companies like GSK, AstraZeneca, Merck, J&J, etc., which should bring-in long-term benefits.
- ✍ Acquisition of Carbogen-AMCIS enables the company to offer the complete range of services in the CRAMS value-chain.
- ✍ Future growth to be led by ramp-up in supplies to Solvay and other MNCs and a gradual improvement in Carbogen-AMCIS performance.

Recent developments

- ✍ NIL.

COMPARATIVE VALUATIONS

		DISHMAN	DIVI'S	SHASUN
P/E (x)	FY08E	21.2	33.2	14.4
	FY09E	16.0	27.4	9.6
P/BV (x)	FY08E	5.1	13.3	1.5
	FY09E	3.9	9.6	1.3
EV/Sales (x)	FY08E	3.7	2.2	0.4
	FY09E	3.0	1.7	0.4
EV/EBITDA (x)	FY08E	17.9	5.5	7.6
	FY09E	13.7	4.3	5.7

SHAREHOLDING PATTERN (%)

	SEP-07	JUN-07	SEP-06
Promoter	63.2	66.4	71.2
Domestic Inst	19.4	18.5	12.5
Foreign	10.8	9.6	11.2
Others	6.6	5.5	5.1

Key investment risks

- ✍ Consolidation amongst customers remains a key risk in the CRAMS industry.
- ✍ Further equity dilution to fund potential acquisitions and currency remains a key risk.
- ✍ Retaining the Carbogen-AMCIS management team is critical for ensuring a smooth integration.

Valuation and view

- ✍ Revenue and EPS CAGR of 30% and 29% expected over FY07-09.
- ✍ One of the key beneficiaries of increased outsourcing by innovator pharmaceutical companies. Maintain Buy with price target of Rs330.

Sector view

- ✍ India is on the threshold of a significant opportunity in the global CRAMS space.
- ✍ Given the high entry barriers, very few players from India are prepared to capitalize on this opportunity resulting in a disproportionate share of revenues for existing CRAMS players.

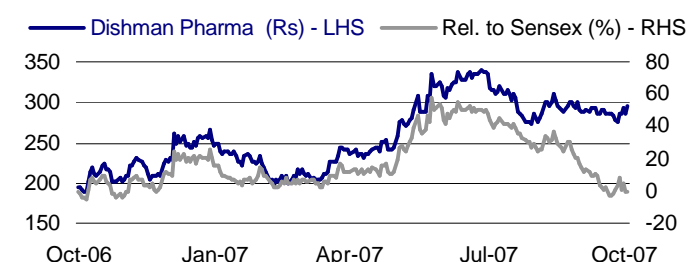
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY08	13.9	15.3	-8.9
FY09	18.5	19.9	-7.1

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
295	330	12.0	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT		(Rs Million)				
Y/E MARCH	2005	2006	2007	2008E	2009E	
Net Sales	1,864	2,761	5,750	8,035	9,735	
Change (%)	113	48.1	108.2	39.7	212	
Total Expenditure	1,360	2,126	4,632	6,364	7,605	
% of Sales	73.0	77.0	80.6	79.2	78.1	
EBITDA	504	635	1,118	1,671	2,130	
Margin (%)	27.0	23.0	19.4	20.8	21.9	
Depreciation	83	120	263	412	456	
EBIT	421	515	854	1,258	1,674	
Int. and Finance Charges	110	59	162	277	277	
Other Income - Rec.	29	38	232	260	200	
PBT before EO Expense	340	493	925	1,241	1,597	
Extra Ordinary Expense/(Inc)	0	0	0	0	0	
PBT after EO Expense	340	493	925	1,241	1,597	
Current Tax	35	33	13	99	80	
Deferred Tax	-27	-2	19	12	16	
Tax Rate (%)	2.3	6.3	3.5	9.0	6.0	
Reported PAT	332	462	893	1,129	1,501	
PAT Adj for EO Items	332	462	893	1,129	1,501	
Change (%)	60.0	39.1	93.3	26.5	32.9	
Margin (%)	17.81	16.73	15.53	14.06	15.42	

BALANCE SHEET		(Rs Million)				
Y/E MARCH	2005	2006	2007	2008E	2009E	
Equity Share Capital	137	137	144	144	144	
Fully Diluted Equity Capital	137	163	163	163	163	
Total Reserves	1,333	1,748	3,039	4,033	5,354	
Net Worth	1,471	1,885	3,183	4,177	5,498	
Deferred liabilities	1	0	109	121	137	
Total Loans	1,183	3,255	5,609	6,297	6,519	
Capital Employed	2,655	5,140	8,902	10,596	12,154	
Gross Block	1,550	2,190	6,079	7,661	8,061	
Less: Accum. Deprn.	321	440	699	1,111	1,567	
Net Fixed Assets	1,229	1,750	5,380	6,550	6,494	
Capital WIP	129	373	650	150	150	
Investments	4	75	140	16	16	
Curr. Assets	1,853	3,746	5,424	6,648	8,822	
Inventory	814	1,082	2,978	3,214	3,894	
Account Receivables	668	863	1,252	2,009	2,434	
Cash and Bank Balance	92	1,352	355	421	1,278	
Loans & Advances	280	449	839	1,004	1,217	
Curr. Liability & Prov.	567	816	2,707	2,783	3,343	
Account Payables	446	657	2,496	2,410	2,921	
Provisions	121	159	211	372	422	
Net Current Assets	1,286	2,930	2,717	3,865	5,480	
Appl. of Funds	2,655	5,140	8,902	10,596	12,154	

E: MOSSt Estimates

RATIOS		(Rs Million)				
Y/E MARCH	2005	2006	2007	2008E	2009E	
Basic (Rs)						
EPS (fully diluted)	4.8	5.7	11.0	13.9	18.5	
Cash EPS (fully diluted)	6.0	7.1	14.2	19.0	24.1	
BV/Share	213	27.3	43.9	57.6	75.9	
DPS	0.5	0.7	1.0	1.6	2.1	
Payout (%)	11.7	11.9	9.6	12.0	12.0	
Valuation (x)						
P/E (fully diluted)		52.0	26.8	21.2	16.0	
Cash P/E (fully diluted)		41.3	20.7	15.5	12.2	
P/BV		10.8	6.7	5.1	3.9	
EV/Sales		9.4	5.1	3.7	3.0	
EV/EBITDA		40.9	26.2	17.9	13.7	
Dividend Yield (%)		0.2	0.3	0.5	0.7	
Return Ratios (%)						
RoE	31.7	27.7	35.4	30.8	31.1	
RoCE	20.5	14.2	15.6	15.8	16.7	
Working Capital Ratios						
Debtor (Days)	128	113	79	89	89	
Creditor (Days)	338	345	-2,261	308	308	
Inventory (Days)	159	143	189	146	146	
Working Capital Turnover (I	234	209	150	156	158	
Leverage Ratio (x)						
Current Ratio	3.3	4.6	2.0	2.4	2.6	
Debt/Equity	0.8	1.7	1.8	1.5	1.2	

CASH FLOW STATEMENT		(Rs Million)				
Y/E MARCH	2005	2006	2007	2008E	2009E	
Oper. Profit/(Loss) before T	504	635	1,118	1,671	2,130	
Interest/Dividends Recd.	29	38	232	260	200	
Direct Taxes Paid	-35	-33	-13	-99	-80	
(Inc)/Dec in WC	-613	-384	-783	-1,082	-758	
CF from Operations	-115	256	553	749	1,492	
EO Expense / (Income)	0	0	0	0	0	
CF from Operating incl	-115	256	553	749	1,492	
(inc)/dec in FA	-303	-890	-4,169	-1,082	-400	
(Pur)/Sale of Investments	0	-71	-65	124	0	
CF from Investments	-303	-961	-4,235	-958	-400	
Issue of Shares	514	7	491	0	0	
(Inc)/Dec in Debt	75	2,072	2,355	688	222	
Interest Paid	-110	-59	-162	-277	-277	
Dividend Paid	-39	-55	-86	-136	-180	
Others	0	0	86	0	0	
CF from Fin. Activity	440	1,965	2,684	275	-236	
Inc/Dec of Cash	22	1,261	-997	66	857	
Add: Beginning Balance	70	92	1,352	355	421	
Closing Balance	92	1,352	355	421	1,278	



For more copies or other information, contact

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

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

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

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

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

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

Disclosure of Interest Statement

Dishman Pharma

- | | |
|---|-----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
| 4. Investment Banking relationship with company covered | Yes |

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