

Wockhardt Limited

Neutral

Negma acquisition fraught with execution risks - ALERT **Rs430.85**

03 May 2007

Wockhardt has acquired Negma Labs in France for an all-cash, no debt deal worth \$265mn. The transaction is valued at 1.8x times CY06 sales of \$150mn and 9.7x EBITDA. The deal is expected to be closed within the next 4-6 weeks. While management was not definitive, it indicated that Negma's revenues have grown 7-8% in the last 2-3 years while profits have grown in "high single digit". Wockhardt will acquire €25-28mn of fixed assets and €50mn of working capital.

Pharmaceuticals

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70% of its sales are from Diacerein for osteoarthritis (brand name ART 50), 10% from Nebivolol (for hypertension) and c. 10% from Troxetium (for varicose veins). Diacerein "compound" patent is expected to expire in 2016. Wockhardt expects ART50 to grow at 7-8% for the next few years with Nebivolol expected to grow exponentially from a low base. In addition, Negma is in negotiations for 2 more in-licensing deals. The company spends 10% of sales on R&D. It does not have any product in advanced clinical studies.

Impact

- The acquisition is to be funded through a \$100mn leverage finance at @Euro LIBOR + 175bp ~ 5.75%. The balance will be initially funded through internal cash balance of \$220mn, but the company plans to dilute equity in 5-6 months to the extent of c. \$150m.
- Wockhardt expects the transaction to be EPS accretive (post funding costs) from the first year itself despite 34% tax rate in France with savings expected in administrative expenses and centralized purchases. It expects to leverage Negma's relationships to launch a generic business in France and also use Negma's 260 people sales-force for other in-licensing deals. It also expects to file combinations for diacerein. However, the management did not articulate its strategy clearly, in our view, possibly because it still had to thrash out the game-plan internally. We also remain unclear on the costs savings especially given that Negma is currently manufacturing its own API and retrenchment costs are high.
- Management's move to enter "brand" segment and keep its options open on future acquisitions in this space, is the reason for our Neutral call, given that we see lot of execution risk.

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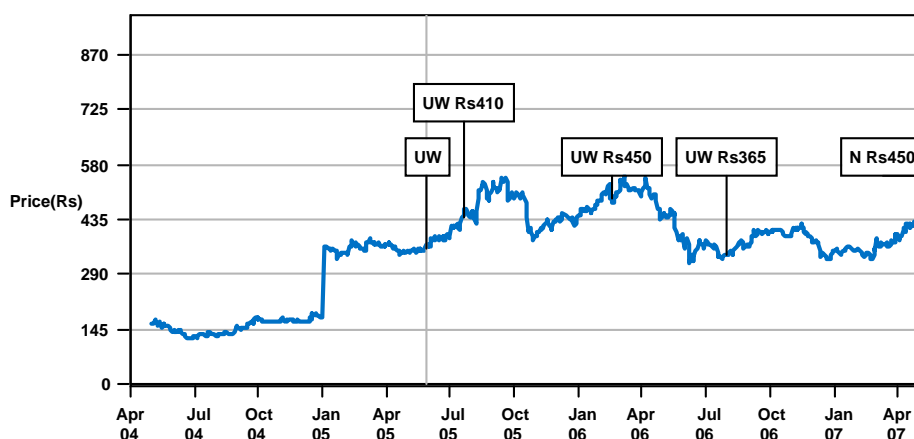
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Wockhardt Limited (WCKH.BO) Price Chart



Date	Rating	Share Price (Rs)	Price Target (Rs)
27-May-05	UW	355.85	-
20-Jul-05	UW	442.65	410.00
16-Feb-06	UW	492.50	450.00
29-Jul-06	UW	341.65	365.00
02-May-07	N	428.85	450.00

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.
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