

July 1, 2010

BUY

Price	Target Price
Rs 779	Rs 852
Sensex	17,509

Price Performance

(%)	1M	3M	6M	12M
Absolute	7	15	15	39
Rel. to Sensex	1	15	15	17

Source: Bloomberg

Stock Details

Sector	Pharmaceuticals
Reuters	DIVI.BO
Bloomberg	DIVI@IN
Equity Capital (Rs mn)	264
Face Value (Rs)	2
No of shares o/s (mn)	132
52 Week H/L (Rs)	784/452
Market Cap (Rs bn/USD mn)	103/2,213
Daily Avg Vol (No of shares)	221191
Daily Avg Turnover (US\$ mn)	3.4

Shareholding Pattern (%)

	M'10	D'09	S'09
Promoters	52.4	52.9	53.0
FII/NRI	16.5	17.4	16.4
Institutions	14.0	14.4	13.9
Private Corp	7.4	6.2	6.7
Public	9.8	9.1	10.1

- **Operating environment is improving and management expects strong growth from 2HFY11E onwards**
- **India's pie in global outsourcing space is likely to increase in next 2-3 years**
- **Carotenoids is the next growth driver for the company**
- **China is no more a threat for Indian CRAMS players**
- **Revised our target price upward from Rs731 to Rs852 (21x FY12E)**

Key Highlights of meeting with Dr. Murali Divi

- Overall operating environment is improving and company has witnessed few of its customers coming back to normalcy level. Going forward, management expects other customers to come back to normal level in next 1-2 quarters.
- Expect business to improve from 2HFY11E onwards and strong growth in FY12E.
- Dr Murali Divi is of the view that current consolidation in the global Pharma space is a big time positive for low cost countries such as India and believes that India's pie will improve in global outsourcing space. He is of the view that China is no more a threat for Indian CRAMS companies because of their quality issue in Heparin and Melamine.
- We believe that Carotenoids will be next growth driver for the company. Though the scale-up of Carotenoids took longer time than anticipated but now management is confident to attain higher revenue from this segment. Carotenoids segment did a revenue of Rs370mn (Rs170mn in Q4FY10) in FY10. Management expects this business to record revenue of Rs750mn in FY11E. We are of the view that since depreciation and interest cost on account of Carotenoids plant is already in P&L account; incremental contribution of Carotenoids will boost the profitability of the company.
- Company is comfortable to maintain 50:50 business mix between generics and CCS segment. Naproxen (contributes 18% of overall sales), Dextromethorphan (contributes 10% of revenues) and Levitracetam (9% of revenue) are few of the key products in the generic space. Company has a robust pipeline of 38 DMF's which will be launched in next few years.
- Company is confident to maintain high operating margins on the back of yield improvement in raw materials and increased contribution of Carotenoids segment.
- Company has indicated a capex outlay of Rs2bn and building facility to manufacture high potency compounds.
- The company has an employee base of 4400 people (1000 plus people with 10 years plus experience) and a research team of 315 people. Company mainly focus on fresh recruitment and this has enabled them to control the personnel cost.

Financials

YE-Mar	Net Sales (Rs mn)	EBITDA (Core)	APAT (%)	EPS (Rs mn)	ROE (%)	P/E (x)	EV/ EBITDA	P/BV (x)	Div. Payout (%)	
FY2009	11,803	4,811	40.8	4,117	32.2	40	23.6	20.3	8.1	10.9
FY2010	9,471	4,107	43.4	3,403	25.6	24	29.7	23.9	6.3	13.4
FY2011E	11,835	4,998	42.2	4,278	32.1	24	23.7	19.5	5.1	14.0
FY2012E	14,533	6,202	42.7	5,400	40.6	25	18.7	15.3	4.1	14.0

Earnings CAGR of 26% over FY10-12E; re-iterate Buy

With recovery in the CRAMS business and low base effect, we expect Divi's to report a earning CAGR of 26% over FY10-12E. We maintain our earning estimates of Rs32.1 and Rs40.6 for FY11E and FY12E respectively and rollover our target price on FY12E. We continue to remain positive on the stock and raise target price to Rs852 (21x FY12E; 3 years average one year forward PE).

Income Statement

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Net Sales (Incl Other Opet Inc)	11803	9471	11835	14533
<i>Growth (%)</i>	14	-20	25	23
Expenses	6992	5364	6837	8332
<i>Growth (%)</i>	12	-23	27	22
Raw Materials	4253	3032	3994	4872
<i>% of sales</i>	36	32	34	34
Employee cost	663	733	858	1038
<i>% of sales</i>	6	8	7	7
Manufacturing exps	808	640	799	980
<i>% of sales</i>	7	7	7	7
R&D	120	105	129	159
<i>% of sales</i>	1	1	1	1
Selling & Dist exps	1148	853	1057	1283
<i>% of sales</i>	10	9	9	9
EBIDTA	4811	4107	4998	6202
<i>Growth (%)</i>	16	-15	22	24
EBIDTA %	40.8	43.4	42.2	42.7
Other income	172	289	496	636
Interest	72	28	43	27
Depreciation	479	515	590	672
Misc. Exp. W/O	0	0	0	0
PBT	4433	3853	4861	6137
Total Tax	316	450	583	737
Effective tax rate (%)	7	12	12	12
PAT (Before E/O items)	4117	3403	4278	5400
<i>Growth (%)</i>	18	-17	26	26
<i>Net Margin (%)</i>	34	35	35	36

Cash Flow

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Pre-tax profit	4482	3853	4861	6138
Depreciation	479	515	590	672
Chg in working cap	(1856)	1047	(1055)	(1209)
Tax paid	(316)	(450)	(583)	(737)
Operating cash Inflow	2789	4966	3812	4865
Capital expenditure	(971)	(919)	(2021)	(1512)
Free Cash Flow	1818	4047	1791	3353
Investments	(1162)	(506)	(500)	(500)
Forex Reserve	0	0	0	0
Equity Capital Raised	68	493	0	0
Loans Taken / (Repaid)	-334	-95	-100	-100
Dividend (incl tax)	(456)	(455)	(599)	(754)
Others	-16	0	0	0
Increase in Misc Exp				
Net chg in cash	-82	3484	593	1999
Opening cash position	142	148	3376	4144
Closing cash position	60	3632	3968	6143

Balance Sheet

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Equity share capital	130	133	133	133
Pref Capital	0	0	0	0
Share Premim	1192	1192	1192	1192
Other Reserves	11092	14531	18210	22857
Minority Interest				
Net worth	12414	15856	19535	24183
Deferred tax liability	434	177	352	513
Secured Loans	473	400	300	200
Unsecured Loans	53	31	31	31
Loan Funds	526	431	331	231
Total Liabilities	13374	16464	20219	24927
Gross Block	7828	8730	10709	12189
Less: Depreciation	1929	2407	2995	3664
Net block	5899	6323	7715	8525
Capital WIP	195	175	214	244
Investment	1718	2224	2724	3224
Current Assets	7672	9430	11691	15565
Inventories	4213	3380	4217	5175
Sundry debtors	2661	1977	2467	3027
Cash & bank balance	148	3376	4144	6303
Loans & advances	650	697	863	1059
Other assets	0	0	0	0
Current liabilities	2110	1688	2125	2630
Current liabilities	1621	1100	1451	1788
Provisions	489	587	674	843
Net current assets	5562	7742	9566	12934
Misc. exp.				
Total Assets	13374	16464	20219	24927

Key Ratios

Y/E, Mar	FY09	FY10	FY11E	FY12E
Per Share Data (Rs)				
EPS (Consolidated)	32.2	25.6	32.1	40.6
Cash EPS (x)	69.0	58.9	73.1	91.2
EBIDTA/share	37.1	30.9	37.5	46.6
Book Value (x)	95.8	119.1	146.7	181.6
EV (Rs.)	98811	98241	97373	95114
Mkt cap	49216	50593	50593	50593
Valuations				
PER (x) (consolidated)	23.6	29.7	23.7	18.7
Price / CEPS (x)	11.0	12.9	10.4	8.3
Price / BV (x)	8.1	6.3	5.1	4.1
EV / Net Sales (x)	8.3	10.4	8.2	6.5
EV / EBITDA (x)(core Activity)	20.3	23.9	19.5	15.3
DPS (Rs)	6.0	6.0	8.0	10.0
Dividend Payout (%)	10.9	13.4	14.0	14.0
Dividend Yield (%)	0.8%	0.8%	1.0%	1.3%
Returns (%)				
RoCE	39%	25%	24%	25%
RoNW	40%	24%	24%	25%
Efficiency ratio				
Debtors T/O	81.2	75.6	75.6	75.6
Creditors T/O	103.3	92.5	121.0	121.3
Working Capital T/O	165.1	167.0	166.2	165.6
Debt/ Equity (x)	0.04	0.03	0.02	0.01
Interest Coverage Ratio	59.8	129.2	102.4	202.9

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