

Ranbaxy Laboratories

Pravastatin delay lowers forecasts

We revise our 2006 projections for Ranbaxy as we see little likelihood of Pravastatin's launch this year. We have rolled over our earnings projections to 2008 and maintain our target price at Rs420 based on 20x 2007F earnings estimates. Hold.

Key forecasts

	FY04A	FY05A	FY06F	FY07F	FY08F
Revenue (Rsm)	52914	51019	59303	71567	77085
EBITDA (Rsm)	8407	1315	9000 ▲	12844 ▲	13191
Reported net profit (Rsm)	6985	2617	4943 ▼	8340 ▼	8369
Normalised net profit (Rsm) ¹	7357	2284	5169	8340	8369
Normalised EPS (Rs)	19.8	6.14	12.9 ▼	20.9 ▼	20.9
Dividend per share (Rs)	8.51	8.50	8.50	10.0	10.0
Dividend yield (%)	2.14	2.14	2.14	2.52	2.52
Normalised PE (x)	20.0	64.7	30.7 ▲	19.1 ▲	19.0
EV/EBITDA (x)	19.8	134.3	19.6	13.7	13.1
Price/book value (x)	5.87	6.04	5.98	5.07	4.43
ROIC (%)	21.2	-0.25	10.2	14.4	13.3

1. Post-goodwill amortisation and pre-exceptional items
Source: Company data, ABN AMRO forecasts
Accounting Standard: Local GAAP

year to Dec, fully diluted

Pravastatin excluded from 2006F numbers

Our earlier estimates included Pravastatin's launch and exclusive 180-day sales of the 80mg version by Ranbaxy. We now push the Pravastatin launch to 2007 as we see little likelihood of the product being on the market within the next 45 days. Consequently, we lower our 2006 EPS forecast by 24% to Rs13. This also includes some adjustment to other income, which has always been a major contributing item to Ranbaxy's earnings. However, forex losses in 2006F have led to a significantly lower number than expected. We also reduce our other income forecasts for 2007 and 2008 to be on the conservative side. We note that every Rs100m variation in our other income forecasts yields an EPS sensitivity of 1%.

Quarterly results are not very encouraging

Ranbaxy's 3Q06 revenue was in line with our expectations but its operating margin disappointed, as we had expected a higher figure born of sales exclusivity for simvastatin and the full impact of the Terapia acquisition. The company has been cutting costs aggressively, both on R&D and SG&A. The past nine-month R&D expense levels are not sustainable, in our view, as these come on the back of fewer ANDA filings and we see expenses bunching up in 4Q06F. Developed market revenue in the European region (the UK, Germany, France and Western Europe) declined 11%, while domestic revenue remained the key growth driver with a 14.5% increase. On the whole, we do not find the results encouraging on a near-term perspective.

Maintain Hold and target price of Rs420

Note that Ranbaxy's 2007 revenue guidance of US\$2bn is short of our estimate by US\$350m-400m, and can be met only by inorganic means, in our view. While this overhang remains, we believe the stock will continue to trade in line with our forecast for the sector at 20x 2007F P/E, given no visible near-term triggers. On our new estimates, we maintain our target price at Rs420 and our Hold recommendation on the stock.

Priced at close of business 13 November 2006. Use of ▲ ▼ indicates that the line item has changed by at least 5%.

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Hold

Absolute performance

n/a

Short term

Neutral

Market relative to region

Pharmaceuticals & Biotechnology

India

Price

Rs397.35

Target price

Rs420.00

Market capitalisation

Rs158.91bn (US\$3.53bn)

Avg (12mth) daily turnover

Rs231.84m (US\$5.13m)

Reuters

RANB.BO

Bloomberg

RBXY IN

Asset allocation

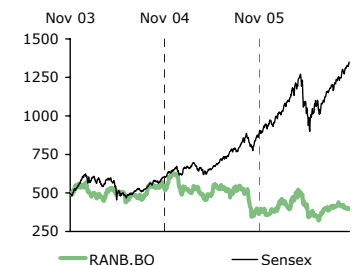
Equities Underweight

Cash Overweight

Bonds Overweight

Price performance (1M) (3M) (12M)

	1M	3M	12M
Price (Rs)	417.9	394.0	382.0
Absolute %	-4.9	0.8	4.0
Rel market %	-9.6	-15.8	-34.2
Rel sector %	-1.1	1.6	-9.2



Stock borrowing: Difficult

Volatility (30-day): 22.06%

Volatility (6-month trend): ↓

52-week range: 530.00-317.10

Sensex: 13399.00

BBG AP Pharm & Biotech: 154.10

Source: ABN AMRO, Bloomberg

Researched by

ABN AMRO Institutional
Equities Team

www.abnamrobroking.co.in

Table 1 : Statins for Ranbaxy in CY07E

	2007F (\$m)
Pravastatin	
180 days exclusivity for 80mg	23
Non exclusivity sales of 80mg for rest of the year	2
Non exclusivity sales of other strengths for full year	13
Simvastatin	
Non exclusivity sales for full year	26
Total statins sales in 2007F	64
% contribution to total 2007F US sales	11%

Source: ABN AMRO forecasts

Table 2 : EPS sensitivity

Exclusivity period in 2007F	180 days	90 days	30 days	0 days
FY07F EPS sensitivity to pravastatin	0.0%	-3.3%	-5.7%	-7.2%
Other income sensitivity	For every +/- Rs100m other income, EPS +/- 1%			

Source: ABN AMRO forecasts

Table 3 : Ranbaxy quarterlies

Year end 31 Dec (Rsm)	1Q05	1Q06	% yoy	2Q05	2Q06	% yoy	3Q05	3Q06	% yoy
Gross sales	11383	12753	12%	13479	14464	7%	13039	16404	26%
Excise	(168)	(122)		(302)	(125)		(209)	(133)	
Net sales	11215	12631	13%	13177	14339	9%	12830	16271	27%
Expenditure	(9754)	(10770)	10%	(10799)	(11095)	3%	(11626)	(12292)	6%
R&D	(806)	(729)	-10%	(1121)	(819)	-27%	(1532)	(1098)	-28%
EBITDA	655	1132	73%	1257	2425	93%	(328)	2881	
D&A	(326)	(427)		(374)	(457)		(355)	(496)	
Other income	651	405		550	(132)		688	(78)	
Interest expense	(138)	(257)		(170)	(277)		(159)	(299)	
PBT	842	853	1%	1263	1559	23%	(154)	2008	-1404%
Tax	(131)	(135)		(247)	(336)		341	(378)	
Net Profit	711	718	1%	1016	1223	20%	187	1630	772%
Minority	(3)	(4)		(3)	(12)		(3)	(4)	
Extraordinary								(226)	
EPS (Rs)	1.9	1.8	-7%	2.7	3.0	11%	0.5	3.5	596%
Margins									
EBITDA margin	5.8%	9.0%		9.5%	16.9%		-2.6%	17.7%	
Net Profit Margin	6.3%	5.7%		7.7%	8.4%		1.5%	8.6%	
Tax rate	-15.6%	-15.8%		-19.6%	-21.6%		NA	-18.8%	

Source: Company data

Sales growth of 26% on the back of full consolidation impact of Terapia and full 90 days of exclusive sales of simvastatin 80mg. LTL growth at 10%

Lesser ANDA filings account for R&D drop; current levels unlikely to be sustained

Other income significantly lower on account of forex losses; a highly uncertain number, which could lead to EPS volatility of 1% for every Rs100m variation

EBITDA margin better by only 80bp qoq despite sales exclusivity for high-margin simvastatin and full consolidation of Terapia (25% EBITDA margin)

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RANBAXY LABORATORIES: KEY FINANCIAL DATA

Income statement

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
Revenue	52914	51019	59303	71567	77085
Cost of sales	-27739	-31548	-32462	-38646	-42397
Operating costs	-16768	-18157	-17841	-20076	-21497
EBITDA	8407	1315	9000	12844	13191
DDA & Impairment (ex gw)	-1215	-1445	-1880	-2239	-2687
EBITA	7192	-129.8	7120	10606	10504
Goodwill (amort/impaird)	n/a	n/a	n/a	n/a	n/a
EBIT	7192	-129.8	7120	10606	10504
Net interest	-81.4	-671.2	-1133	-913.2	-991.1
Associates (pre-tax)	n/a	n/a	n/a	n/a	n/a
Forex gain / (loss)	n/a	n/a	n/a	n/a	n/a
Exceptionals (pre-tax)	-371.9	333.1	-226.0	0.00	0.00
Other pre-tax items	2153	2413	345.0	515.3	739.1
Reported PTP	8892	1945	6106	10208	10252
Taxation	-1881	697.6	-1140	-1837	-1845
Minority interests	-25.5	-25.5	-24.0	-30.0	-37.5
Exceptionals (post-tax)	n/a	n/a	n/a	n/a	n/a
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	6985	2617	4943	8340	8369
Normalised Items Excl. GW	-371.9	333.1	-226.0	0.00	0.00
Normalised net profit	7357	2284	5169	8340	8369

Source: Company data, ABN AMRO forecasts

year to Dec

Balance sheet

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
Cash & market secs (1)	1339	2430	3126	6020	11086
Other current assets	34130	30849	33727	40470	43928
Tangible fixed assets	18170	26187	26681	26557	26048
Intang assets (incl gw)	n/a	n/a	n/a	n/a	n/a
Oth non-curr assets	183.8	2920	3020	3150	3250
Total assets	53823	62386	66554	76197	84311
Short term debt (2)	1100	n/a	n/a	n/a	n/a
Trade & oth current liab	19168	15008	16128	19333	21014
Long term debt (3)	7427	20043	21045	22830	24778
Oth non-current liab	841.9	2699	2599	2499	2399
Total liabilities	28537	37750	39772	44662	48191
Total equity (incl min)	25286	24636	26782	31534	36120
Total liab & sh equity	53823	62386	66554	76197	84311
Net debt (2+3-1)	7188	17613	17919	16810	13692

Source: Company data, ABN AMRO forecasts

year ended Dec

Cash flow statement

Rsm	FY04A	FY05A	FY06F	FY07F	FY08F
EBITDA	8407	1315	9000	12844	13191
Change in working capital	-4216	-648.4	-1758	-3538	-1778
Net interest (pd) / rec	2072	1742	-788.0	-397.9	-252.0
Taxes paid	-1881	697.6	-1140	-1837	-1845
Other oper cash items	-371.9	302.0	-226.0	n/a	n/a
Cash flow from ops (1)	4010	3407	5089	7071	9316
Capex (2)	-5285	-9508	-2360	-2116	-2177
Disposals/(acquisitions)	0.00	0.00	0.00	0.00	0.00
Other investing cash flow	-3340	12.1	-48.3	-30.0	0.00
Cash flow from invest (3)	-8626	-9496	-2408	-2146	-2177
Incr / (decr) in equity	166.7	3.30	0.00	0.00	0.00
Incr / (decr) in debt	2677	11515	1002	1785	1948
Ordinary dividend paid	-3158	-3614	-2821	-3617	-3821
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	-471.6	-724.9	-165.7	-200.0	-200.0
Cash flow from fin (5)	-785.3	7179	-1984	-2032	-2073
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Inc/(decr) cash (1+3+5+6)	-5401	1091	696.4	2894	5066
Equity FCF (1+2+4)	-1275	-6101	2729	4956	7139

Lines in bold can be derived from the immediately preceding lines.

Source: Company data, ABN AMRO forecasts

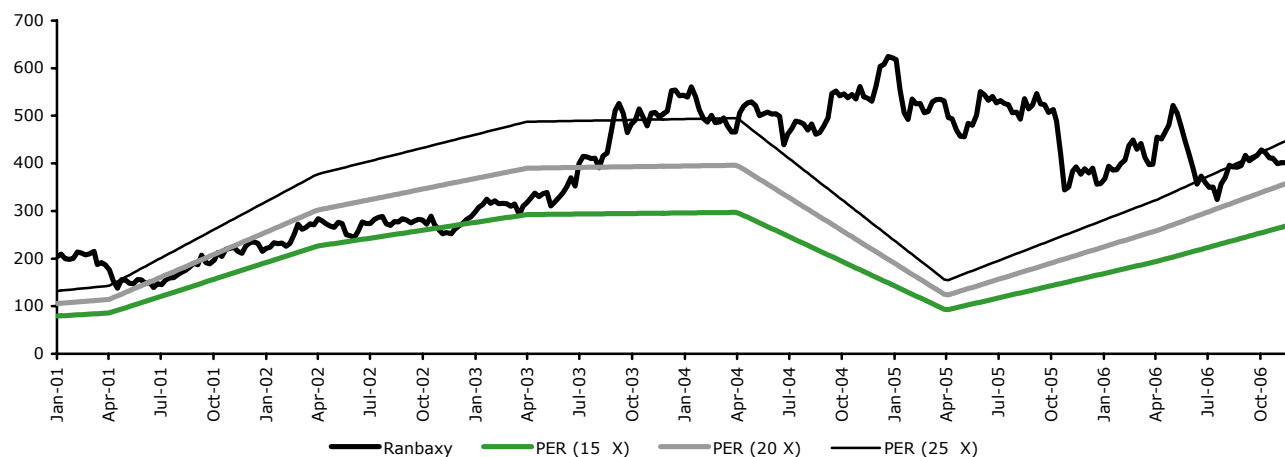
year to Dec

RANBAXY LABORATORIES: PERFORMANCE AND VALUATION

Standard ratios	Ranbaxy Lab					Dr Reddy's Laboratories			Sun Pharmaceutical		
Performance	FY04A	FY05A	FY06F	FY07F	FY08F	FY07F	FY08F	FY09F	FY06F	FY07F	FY08F
Sales growth (%)	17.6	-2.73	16.2	20.7	7.71	134.6	-15.3	17.4	39.3	20.0	15.3
EBITDA growth (%)	10.2	-84.4	584.6	42.7	2.70	426.2	-11.0	27.2	19.4	23.6	17.1
EBIT growth (%)	11.7	-95.5	1662	48.9	-0.95	602.7	-14.9	33.4	15.9	27.1	18.0
Normalised EPS growth (%)	1.58	-69.0	110.4	61.4	0.35	428.5	-10.9	38.5	44.7	17.7	8.78
EBITDA margin (%)	16.0	2.58	15.2	17.9	17.1	20.2	21.3	23.0	31.2	32.2	32.7
EBIT margin (%)	13.7	-0.25	12.0	14.8	13.6	15.4	15.5	17.6	27.4	29.0	29.7
Net profit margin (%)	14.0	4.48	8.72	11.7	10.9	12.2	12.8	15.1	36.0	35.3	33.3
Return on avg assets (%)	15.4	4.72	9.18	12.5	11.3	9.98	8.21	10.7	13.5	14.2	14.8
Return on avg equity (%)	31.5	9.21	20.2	28.8	24.9	27.3	19.8	23.0	42.3	38.7	33.3
ROIC (%)	21.2	-0.25	10.2	14.4	13.3	11.6	8.78	11.5	23.2	24.3	26.7
ROIC - WACC (%)	11.0	-11.1	-0.68	3.55	0.00	0.74	-2.10	0.67	13.0	14.1	16.5
				<i>year to Dec</i>			<i>year to Mar</i>			<i>year to Mar</i>	
Valuation											
EV/sales (x)	3.17	3.46	2.98	2.46	2.24	1.42	1.57	1.20	12.7	10.5	8.89
EV/EBITDA (x)	19.8	134.3	19.6	13.7	13.1	7.03	7.37	5.22	40.5	32.5	27.2
EV/EBITDA @ tgt price (x)	20.8	141.2	20.7	14.4	13.8	8.06	8.53	6.13	30.5	24.4	20.3
EV/EBIT (x)	23.1	n/m	24.8	16.6	16.4	9.23	10.1	6.84	46.3	36.1	29.9
EV/invested capital (x)	4.99	3.93	3.74	3.46	3.31	1.44	1.33	1.18	8.84	8.16	7.35
Price/book value (x)	5.87	6.04	5.98	5.07	4.43	4.28	3.61	3.00	12.4	10.3	7.85
Equity FCF yield (%)	-0.86	-4.13	1.72	3.12	4.49	0.08	4.51	6.35	0.95	2.65	2.71
Normalised PE (x)	20.0	64.7	30.7	19.1	19.0	17.6	19.7	14.3	34.2	29.0	26.7
Norm PE @tgt price (x)	21.2	68.4	32.5	20.1	20.1	21.0	23.6	17.0	25.4	21.6	19.9
Dividend yield (%)	2.14	2.14	2.14	2.52	2.52	0.63	0.76	1.40	0.63	0.72	0.75
				<i>year to Dec</i>			<i>year to Mar</i>			<i>year to Mar</i>	
Per share data											
Tot adj dil sh, ave (m)	371.1	371.8	399.9	399.9	399.9						
Reported EPS (INR)	18.8	7.04	12.4	20.9	20.9						
Normalised EPS (INR)	19.8	6.14	12.9	20.9	20.9						
Dividend per share (INR)	8.51	8.50	8.50	10.0	10.0						
Equity FCF per share (INR)	-3.44	-16.4	6.82	12.4	17.9						
Book value per sh (INR)	67.7	65.8	66.5	78.3	89.7						
				<i>year to Dec</i>							
Solvency											
Net debt to equity (%)									28.4	71.5	66.9
Net debt to tot ass (%)									13.4	28.2	26.9
Net debt to EBITDA									0.85	13.4	1.99
Current ratio (x)									1.75	2.22	2.29
Operating CF int cov (x)									-1.84	-0.56	8.90
Dividend cover (x)									2.33	0.72	2.09
											<i>year to Dec</i>

Priced as follows: RANB.BO - Rs397.35; REDY.BO - Rs795.10; SUN.BO - Rs945.10
Source: Company data, ABN AMRO forecasts

RANBAXY LABORATORIES: 1-YEAR FORWARD PE BAND CHART



Source: Bloomberg, ABN AMRO

Ranbaxy Laboratories

Company description

Ranbaxy is the biggest domestic pharmaceutical company in India. It is recognised for its research-based approach and accent on exports. It is now rapidly making significant inroads in the advanced markets. The company is ramping up its filings and registrations and is making a push into the US, which is the world's biggest generic market. Ranbaxy is also bringing out novel drug delivery systems and was the first Indian company to license a product in this field to Bayer AG.

Hold

Price relative to country



Strategic analysis

Average SWOT company score: 4

Revenue breakdown, 2006F

Strengths

Drug discovery research. US FDA-approved manufacturing facilities. Strong pipeline of generic drugs in advanced markets. **4**

Weaknesses

The company's high exposure to matured anti-infective segments in the domestic market is affecting growth. **2**

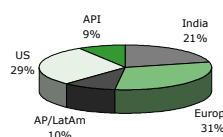
Opportunities

The substantial US market for generics, other non-regulated markets such as Brazil, Russia, CIS, China and India. **5**

Threats

Increased competition in the generics segment in the US. Slowdown in the number of drugs going off-patent in future. **3**

Scoring range is 1-5 (high score is good)



Source: ABN AMRO forecasts

Market data

Headquarters

19, Nehru Place, New Delhi - 110 019, India.

Website

ranbaxy.com

Shares in issue

399.9m

Freefloat

68%

Majority shareholders

Promoters and Associates (32%)

India

Country view

Neutral

Country rel to Asia Pacific

The market looks expensive, but we believe it will remain supportive when regional funds seek a domestically-driven home with continuing robust earnings growth. The ABN AMRO Indian PMI suggests the economy is still powering ahead despite the global headwinds, thanks to its domestically-oriented economic structure. At the sector level, we still like autos, software and construction-related stocks.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.



Competitive position

Average competitive score: 4+

Broker recommendations

Supplier power

Strong backward integration, FDA-approved manufacturing facilities, hence no problems in raw material supplies. **5+**

Barriers to entry

Strong R&D background focusing on new drug delivery technology. Strength in chemical synthesis and distribution network difficult to replicate. **4+**

Customer power

Key products have pricing power. But in the generics market of the West, 'the lower the price, the better the market share'. **3+**

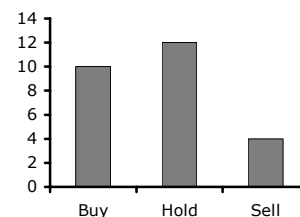
Substitute products

Older products are substitutable. Hence, need to innovate constantly in bringing complex products to market. **3+**

Rivalry

Strong competition from a number of players, who are well entrenched in the advanced markets Ranbaxy is targeting. **3+**

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse



Source: Bloomberg