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Q1 CY07  
Result Update

# Glaxo SmithKline Pharma

Outperformer

Rs 1,162

April 30, 2007

## Healthy Margin

| Company Details  |                | Result Snapshot  |        |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
|--|----------------|--|--------|-------------------|--|--|--|-----|----|----|-----|----------|-----|-----|--------|-----------------------|-----|
| Market Cap:  | Rs 98,421m     | <p>Glaxo SmithKline Pharmaceuticals (GSK) has reported satisfactory results for Q1FY07. The on-going business grew at a slower pace of 5% due to the base effect.</p> <p>The operating margin improved by 130bps—from 33.1% to 34.4%. Both pharma and other businesses have reported improved margins.</p> <p>Though the current quarter was an exceptional quarter, the company is likely to report double-digit growth in the current year.</p> <p>The CMP of Rs 1162 discounts the CY07E EPS of Rs 52.0 by 22.4x and the CY08E EPS of Rs 59.7 by 19.5x. We expect the scrip to be Outperformer.</p> |        |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| 52-Week High/Low:  | Rs 1,495 / 891 |  |        |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| Bloomberg Code:  | GLXO@IN        |  |        |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| Reuters Code:  | GLAX.BO / NS   |  |        |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| Shares O/s:  | 85m            |  |        |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| Average Volume<br>(3 months):  | 67,833 shares  |  |        |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| <table border="1"> <thead> <tr> <th colspan="4">Price Performance</th> </tr> <tr> <th>(%)</th> <th>1m</th> <th>3m</th> <th>12m</th> </tr> </thead> <tbody> <tr> <td>Absolute</td> <td>7.4</td> <td>2.8</td> <td>(15.8)</td> </tr> <tr> <td>Relative to<br/>Sensex</td> <td>0.2</td> <td>5.5</td> <td>(33.1)</td> </tr> </tbody> </table> |                |  |        | Price Performance |  |  |  | (%) | 1m | 3m | 12m | Absolute | 7.4 | 2.8 | (15.8) | Relative to<br>Sensex | 0.2 |
| Price Performance  |                |  |        |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| (%)  | 1m             | 3m   | 12m    |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| Absolute   | 7.4            | 2.8  | (15.8) |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |
| Relative to<br>Sensex  | 0.2            | 5.5  | (33.1) |                   |  |  |  |     |    |    |     |          |     |     |        |                       |     |

## Quarterly Table

(Rs m)

| Y/e March                | Q1CY07       | Q1CY06       | yoy gr. (%)  | Q4CY06       | qoq gr. (%) |
|--------------------------|--------------|--------------|--------------|--------------|-------------|
| <b>Net sales</b>         | <b>4,215</b> | <b>4,261</b> | <b>(1.1)</b> | <b>3,207</b> | <b>31.4</b> |
| <b>Expenditure</b>       |              |              |              |              |             |
| Raw materials            | 1,701        | 1,784        | (4.7)        | 1,295        | 31.4        |
| <i>As % of net sales</i> | <i>40.4</i>  | <i>41.9</i>  |              | <i>40.4</i>  |             |
| Personnel expenses       | 402          | 371          | 8.4          | 353          | 13.9        |
| <i>As % of net sales</i> | <i>9.5</i>   | <i>8.7</i>   |              | <i>11.0</i>  |             |
| Other expenses           | 662          | 695          | (4.7)        | 741          | (10.7)      |
| <i>As % of net sales</i> | <i>15.7</i>  | <i>16.3</i>  |              | <i>23.1</i>  |             |
| Total Expenditure        | 2,765        | 2,850        | (3.0)        | 2,389        | 15.7        |
| <b>OPBDIT</b>            | <b>1,450</b> | <b>1,411</b> | <b>2.8</b>   | <b>818</b>   | <b>77.3</b> |
| <i>OP Margin (%)</i>     | <i>34.4</i>  | <i>33.1</i>  |              | <i>25.5</i>  |             |
| Other income             | 272          | 222          | 22.5         | 300          | (9.3)       |
| <b>PBDIT</b>             | <b>1,722</b> | <b>1,633</b> | <b>5.5</b>   | <b>1,118</b> | <b>54.0</b> |
| Depreciation             | 37           | 38           | (2.6)        | 41           | (9.8)       |
| <b>PBT</b>               | <b>1,685</b> | <b>1,595</b> | <b>5.6</b>   | <b>1,077</b> | <b>56.5</b> |
| Prov. For tax            | 573          | 561          | 2.1          | 391          | 46.5        |
| <i>% of PBT</i>          | <i>34.0</i>  | <i>35.2</i>  |              | <i>36.3</i>  |             |
| <b>PAT</b>               | <b>1,112</b> | <b>1,034</b> | <b>7.5</b>   | <b>686</b>   | <b>62.1</b> |
| Extraordinary item       | -            | (22)         | NA           | 4            |             |
| <b>Reported PAT</b>      | <b>1,112</b> | <b>1,056</b> | <b>5.3</b>   | <b>682</b>   | <b>63.0</b> |

(Stock price as on April 30, 2007)



## Result Highlights

GSK has reported satisfactory results for Q1 CY07, with a 1% decline in net sales—from Rs 4.26bn to Rs 4.22bn due to the base effect. In the previous quarter Q1CY06, the company has reported a top line growth of 54% due to the VAT related issues and hence the results should be viewed with respect to the higher base. Moreover, GSK hived its animal healthcare business (AHC) in June'06 to Virbac Animal Health India Private Limited for Rs 2.07bn. The Q1CY07 results are without AHC business, which had quarterly sales of around Rs 200m. Due to these two re-structuring, the on-going business grew by 5.1% YoY during the quarter.

Notably, the excise duty during the quarter was up by 19% --from Rs 308m to Rs 365m mainly due to reduction in out-sourcing of finished products.

### Healthy margin

The company's operating margin improved by 130bps—from 33.1% to 34.4% mainly due to the decline in the material cost and other expenses. GSK's material cost declined by 150bps—from 41.9% to 40.4% due to the change in product mix after hiving off the AHC division. Personnel cost was up by 80bp—from 8.7% to 9.5% of net sales—due to the rise in the salary and perquisites. 'Other expenses' declined by 60bp—from 16.3% to 15.7% of net sales—due to the operational efficiencies and strict control on the expenses.

The PBIT margin for the pharma business improved by 110bps—from 37.3% to 38.4% whereas that of other businesses (consisting of fine chemicals, diagnostics, laboratory equipments and exports) was up by 360bps—from 17.9% to 21.5%. This indicates that both pharma and other businesses are doing well.

GSK enjoys a very high EBIDTA margin of 40.8%. The company derived Rs 101m interest income during the quarter from the treasury operations. GSK has a cash and cash equivalent of Rs 12.0bn at the end of Q1CY07, which is effectively deployed.

### Debt-free company

This debt-free company earned 23% higher income --from Rs 222m to Rs 272m during the quarter mainly from the treasury operations. GSK's depreciation for the quarter dropped by 3%--from Rs 38m to Rs 37m with the hiving of AHC business. Its tax provisioning declined --from 35.2% to 34.0% of PBT. Net profit (before EO items) improved by 8%—from Rs 1.03bn to Rs 1.11bn. GSK reported 10% improvement in net profit (after EO items) for the quarter.

### Plans acquisition

GSK is actively scouting for brands/companies in the domestic market, as it is cash rich. Due to the high valuations for the brands and companies, it is unable to finalise any deal.

## Financials and Valuations

We expect the company to report a 12% top line growth in CY07 and 11% in CY08 due to its well-established brands and introduction of new products. GSK's new products have contributed 10% to the CY06 sales and are performing well in the domestic market. With the introduction of new products and other in-licensing opportunities, the company will be in a position to maintain a double-digit growth.



GSK enjoys high operating margin of 34.4% and EBITDA margin of 40.8%. It is among the few pharma companies to have such high margins. With the stable business model and high treasury income, the company is likely to maintain high margins in the future.

At the CMP of Rs 1162, the stock trades at 22.4x CY07E EPS of Rs 52.0 and 19.5x CY08E EPS of Rs 59.7. We expect the scrip to be an Outperformer.

### Key Figures

| Y/e Dec                | CY05        | CY06        | CY07E       | CY08E       |
|------------------------|-------------|-------------|-------------|-------------|
| Revenues (Rs m)        | 14,853      | 15,530      | 17,359      | 19,288      |
| EBITDA (Rs m)          | 4,280       | 4,760       | 5,513       | 6,285       |
| <i>Margins (%)</i>     | <i>28.8</i> | <i>30.7</i> | <i>31.8</i> | <i>32.6</i> |
| PAT (before EO) (Rs m) | 3,063       | 3,618       | 4,402       | 5,054       |
| EPS (Rs)               | 36.2        | 42.7        | 52.0        | 59.7        |
| PER (x)                | 32.1        | 27.2        | 22.4        | 19.5        |
| EV / E (x)             | 19.9        | 17.2        | 14.3        | 12.5        |
| EV / Sales (x)         | 6.6         | 6.3         | 5.7         | 5.1         |
| <i>RoCE (%)</i>        | <i>52.7</i> | <i>52.8</i> | <i>52.7</i> | <i>52.2</i> |
| <i>RoE (%)</i>         | <i>53.6</i> | <i>50.9</i> | <i>33.9</i> | <i>33.6</i> |

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