

Ranbaxy Laboratories Ltd

Results in line, base business stable; Maintain Buy

Ranbaxy's (RBXY) Q2CY10 results were broadly in line with our estimates as the company reported growth across most of its business verticals. Reported numbers, however, included one-off revenues from the generic *Valtrex*. RBXY has a very strong FTF pipeline but has been unable to fully monetise the same due to manufacturing issues – this has had a negative impact on revenue realisation, leading to mixed results for various drugs launched by the company. The FDA issue is now 22 months old, and with incremental time available for site transfer, the chances of success should increase. The base business, currently facing pressure on profitability (on restructuring and incremental regulatory costs), should also improve, going ahead. Valuations (2.4x CY11E EV/Sales) offer limited downside from current levels. We maintain our Buy rating on the stock with a target price of Rs 520 (17% upside).

Benefits from Para-IV generic *Valtrex* exclusivity: RBXY reported a 17% YoY revenue growth during Q2CY10, mainly driven by the benefits derived from exclusivity of the generic *Valtrex* in the US market. The company reported a core EBITDA of Rs 3.7bn (and a margin of 17%) vis-à-vis a loss of Rs 305mn in the year-ago quarter – again, driven by the high-margin Para-IV product. This also enabled the company to turnaround at the net level (adj. PAT recovered to Rs 4.6bn from a loss of Rs 3.8bn last year).

Base business recovery on track: Excluding the impact on one-offs (Para-IV), RBXY reported recovery in most of its formulations verticals. However, lower API sales and absence of revenues from divested businesses led to a 4% decline in base business sales. The company's EBITDA margin, adjusted for high-margin one-offs, turned from negative to positive over the last year. Margin recovery was also seen on a QoQ basis.

Concall takeaways: 1. Post RBXY's meeting with USFDA officials, we will have more clarity on the re-inspection of the company's *Dewas* facility. 2. The earlier ignored domestic formulations business is seeing a 10% plus growth – this would significantly increase from the second half of the year as initiatives of project *Viraat* become productive. 3. Transfer of R&D assets to the parent will fetch over Rs 2bn plus and save US\$ 20mn as annualised R&D spend for the company.

Concerns priced in – Buy: The stock is trading at 2.4x CY11E EV/sales, cheapest amongst India's top four generic players. These valuations, we believe, factor in most of the concerns. We ascribe 2.6x as a multiple (the avg. multiple for global generics companies) which is RBXY's historic median multiple and a 60% discount to the FY12E multiple of the sector leader. NPV of FTF opportunities works out to Rs 150. Given the uncertainties on the execution front, we value the NPV at a 30% discount to Rs 100. Our target price stands at Rs 520. Buy.

Financial highlights

(Rs mn)	CY08	CY09	CY10E	CY11E
Revenue	72,245	73,294	85,331	87,750
Growth (%)	8.7	1.5	16.4	2.8
Adj net income	9,046	(459)	12,884	14,139
Growth (%)	240.5	NA	NA	9.7
FDEPS (Rs)	21.5	(1.1)	30.6	33.6
Growth (%)	202.2	NA	NA	9.7

Profitability and return ratios

(%)	CY08	CY09	CY10E	CY11E
EBITDA margin	5.5	6.1	17.7	19.2
EBIT margin	1.5	2.4	13.5	14.8
Adj PAT margin	12.5	(0.6)	15.1	16.1
ROE	25.5	(1.1)	25.8	23.5
ROIC	1.2	2.0	11.8	12.7
ROCE	1.2	1.7	10.7	11.9

What's New? Target Rating Estimates

CMP	TARGET	RATING	RISK
Rs 445	Rs 520	BUY	HIGH

BSE	NSE	BLOOMBERG
500359	RANBAXY	RBXY IN

Company data

Market cap (Rs mn / US\$ mn)	187,278 / 4,003
Outstanding equity shares (mn)	421
Free float (%)	36.1
Dividend yield (%)	0.0
52-week high/low (Rs)	538 / 257
2-month average daily volume	796,513

Stock performance

Returns (%)	CMP	1-mth	3-mth	6-mth
Ranbaxy	445	(3.7)	(1.8)	9.2
BSE HC	5,548	(3.5)	4.7	16.5
Sensex	18,220	2.2	5.1	14.4

Valuation matrix

(x)	CY08	CY09	CY10E	CY11E
EV/EBITDA @ CMP	53.5	47.5	14.0	12.6
EV/Sales @ CMP	2.9	2.9	2.5	2.4





Result highlights

Fig 1 - Quarterly performance

Reported	Q2CY10	Q2CY09	% Chg YoY	Q1CY10	% Chg QoQ
Sales	20,988	17,919	17	24,867	(16)
EBITDA	3,652	(305)	NA	7,438	(51)
<i>EBITDA margins</i>	17.4	(1.7)	<i>1,910bps</i>	0.3	<i>1,710bps</i>
Adj. PAT	4,575	(3,756)	NA	4,436	3
One timers					
Sales	3,868			8,085	(52)
EBITDA	3,558			7,438	(52)
<i>EBITDA margins</i>	92.0			92.0	
Adj. PAT	2,823			5,902	(52)
Base-Business					
Sales	17,120	17,919	(4)	16,782	2
EBITDA	93	(305)	NA	(0.3)	NA
<i>EBITDA margins</i>	0.5	(1.7)	225bps	(0.0)	55bps
Adj. PAT	1,751	(3,756)	NA	(1,466)	NA

Source: Company, RCML Research

Valtrex sales boosted reported topline growth in Q2CY10



Consolidated financials

Profit and Loss statement

Y/E Dec (Rs mn)	CY08	CY09	CY10E	CY11E
Revenues	72,245	73,294	85,331	87,750
Growth (%)	8.7	1.5	16.4	2.8
EBITDA	3,944	4,448	15,116	16,810
Growth (%)	(32.1)	12.8	239.8	11.2
Depreciation & amortisation	2,825	2,676	3,563	3,783
EBIT	1,119	1,772	11,553	13,027
Growth (%)	(69.1)	58.4	552.0	12.8
Interest	2,055	710	791	853
Other income	4,494	5,612	5,577	5,784
EBT	3,558	6,673	16,338	17,958
Income taxes	(5,651)	6,991	3,298	3,647
Effective tax rate (%)	(158.8)	104.8	20.2	20.3
Extraordinary items	18,637	(3,392)	36	39
Min into / inc from associates	84	109	120	132
Reported net income	(9,512)	2,965	12,884	14,139
Adjustments	18,637	(3,392)	36	39
Adjusted net income	9,046	(459)	12,884	14,139
Growth (%)	240.5	NA	NA	9.7
Shares outstanding (mn)	420.4	420.4	420.4	420.4
FDEPS (Rs) (adj)	21.5	(1.1)	30.6	33.6
Growth (%)	202.2	NA	NA	9.7
DPS (Rs)	-	2.5	5.0	5.0

Cash flow statement

Y/E Dec (Rs mn)	CY08	CY09	CY10E	CY11E
Net income + Depreciation	(6,687)	5,641	16,448	17,922
Non-cash adjustments	7,525	(7,533)	2,580	132
Changes in working capital	(2,387)	271	(3,628)	(3,195)
Cash flow from operations	(1,549)	(1,621)	15,399	14,860
Capital expenditure	(5,749)	(5,221)	(4,000)	(4,000)
Change in investments	(3,569)	523	-	-
Other investing cash flow	2,350	5,349	-	-
Cash flow from investing	(6,968)	652	(4,000)	(4,000)
Issue of equity	36,146	13	-	-
Issue/repay debt	(4,497)	(4,460)	-	(22,125)
Dividends paid	(3,169)	(2,239)	-	-
Other financing cash flow	(1,594)	1,464	-	(2,459)
Change in cash & cash eq	18,369	(6,192)	11,399	(13,725)
Closing cash & cash eq	23,956	12,416	23,632	9,774

Economic Value Added (EVA) analysis

Y/E Dec	CY08	CY09	CY10E	CY11E
WACC (%)	9.2	9.2	9.2	9.2
ROIC (%)	1.2	2.0	11.8	12.7
Invested capital (Rs mn)	68,767	76,516	80,581	83,993
EVA (Rs mn)	(5,443)	(5,509)	2,107	2,951
EVA spread (%)	(7.9)	(7.2)	2.6	3.5

Balance sheet

Y/E Dec (Rs mn)	CY08	CY09	CY10E	CY11E
Cash and cash eq	23,956	12,416	23,632	9,774
Accounts receivable	13,310	18,399	19,338	20,781
Inventories	19,643	18,407	19,346	20,789
Other current assets	8,191	10,863	11,219	11,730
Investments	5,432	5,407	5,407	5,407
Gross fixed assets	61,942	62,786	66,786	70,786
Net fixed assets	44,900	44,905	45,342	45,559
CWIP	4,707	6,231	6,231	6,231
Intangible assets	-	-	-	-
Deferred tax assets, net	12,476	4,906	4,906	4,906
Other assets	-	-	-	-
Total assets	132,616	121,535	135,421	125,177
Accounts payable	11,039	14,394	13,083	13,267
Other current liabilities	28,761	18,117	18,033	18,051
Provisions	6,083	8,602	10,998	10,998
Debt funds	42,849	36,295	36,295	18,320
Other liabilities	2,678	2,452	2,452	2,452
Equity capital	2,102	2,102	2,102	2,102
Reserves & surplus	39,104	39,573	52,458	59,987
Shareholder's funds	41,206	41,675	54,560	62,089
Total liabilities	132,616	121,535	135,421	125,177
BVPS (Rs)	102.2	103.3	134.0	151.9

Financial ratios

Y/E Dec	CY08	CY09	CY10E	CY11E
Profitability & Return ratios (%)				
EBITDA margin	5.5	6.1	17.7	19.2
EBIT margin	1.5	2.4	13.5	14.8
Net profit margin	12.5	(0.6)	15.1	16.1
ROE	25.5	(1.1)	25.8	23.5
ROCE	1.2	1.7	10.7	11.9
Working Capital & Liquidity ratios				
Receivables (days)	71	85	96	95
Inventory (days)	207	219	239	251
Payables (days)	112	147	174	165
Current ratio (x)	1.6	1.8	2.4	2.0
Quick ratio (x)	0.9	0.9	1.4	1.0
Turnover & Leverage ratios (x)				
Gross asset turnover	1.2	1.1	1.1	1.1
Total asset turnover	0.6	0.5	0.6	0.6
Interest coverage ratio	0.5	2.5	14.6	15.3
Adjusted debt/equity	1.0	0.8	0.6	0.3
Valuation ratios (x)				
EV/Sales	2.9	2.9	2.5	2.4
EV/EBITDA	53.5	47.5	14.0	12.6
P/E	20.7	-	14.5	13.2
P/BV	4.4	4.3	3.3	2.9



Quarterly trend

Particulars	Q2CY09	Q3CY09	Q4CY09	Q1CY10	Q2CY10
Revenue (Rs mn)	17,919	17,163	22,664	24,867	20,988
YoY growth (%)	(2)	(9)	19	60	17
QoQ growth (%)	15	(4)	32	10	(16)
EBITDA (Rs mn)	(305)	732	5,717	7,714	3,652
EBITDA margin (%)	(2)	4	25	31	17
Adj net income (Rs mn)	(3,756)	1,380	5,364	5,113	4,575
YoY growth (%)	-	-	-	41	(222)
QoQ growth (%)	-	-	-	(5)	(11)

DuPont analysis

(%)	CY07	CY08	CY09	CY10E	CY11E
Tax burden (Net income/PBT)	0.5	2.5	(0.1)	0.8	0.8
Interest burden (PBT/EBIT)	1.4	3.2	3.8	1.4	1.4
EBIT margin (EBIT/Revenues)	0.1	0.0	0.0	0.1	0.1
Asset turnover (Revenues/Avg TA)	0.7	0.6	0.6	0.7	0.7
Leverage (Avg TA/Avg equity)	3.3	3.2	2.9	2.6	2.2
Return on equity	9.9	25.5	(1.1)	25.8	23.5

Company profile

Ranbaxy is one of the leading pharma company in India. The company manufactures generic formulations and APIs and has presence in several countries. In 2008, Japan based Daiichi Sankyo acquired Ranbaxy from the promoter group. The company has a very strong product pipeline, particularly for the US market.

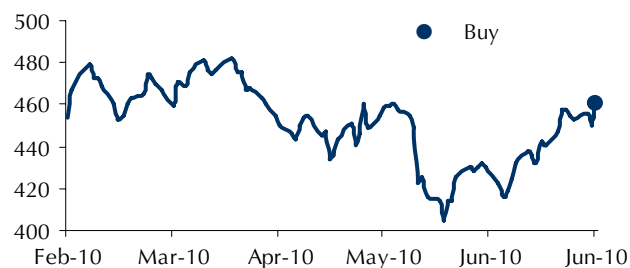
Shareholding pattern

(%)	Dec-09	Mar-10	Jun-10
Promoters	63.9	63.9	63.9
FII's	6.8	7.6	6.9
Banks & FI's	11.8	11.6	11.6
Public	17.5	16.9	17.6

Recommendation history

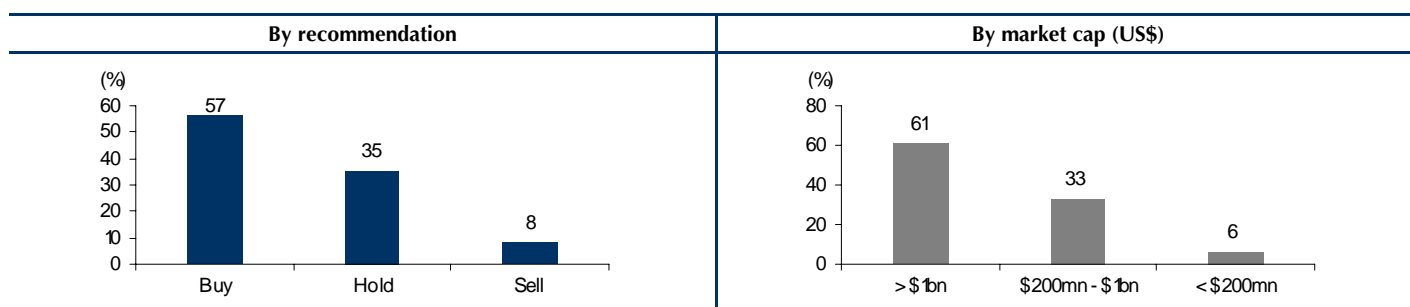
Date	Event	Reco price	Tgt price	Reco
5-Jul-10	Initiating coverage	460	520	Buy
12-Aug-10	Results Review	445	520	Buy

Stock performance





Coverage Profile



Recommendation interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and -5%
Sell	Less than -5%

Recommendation structure changed with effect from March 1, 2009

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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