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India Pharmaceuticals Sector

Pharmaceuticals & healthcare: India

Positive

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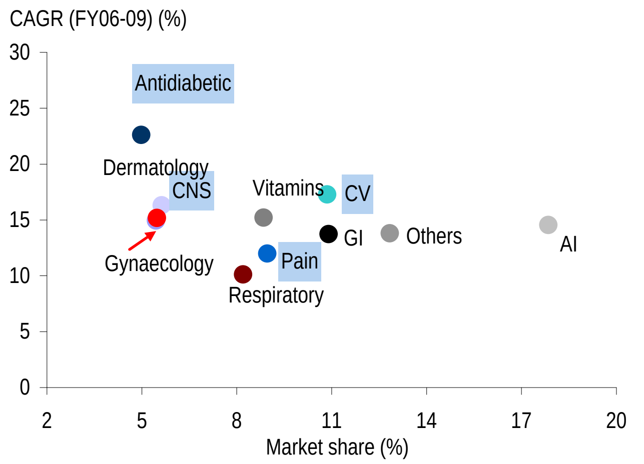
Pharma Investor Day: key highlights

Summary

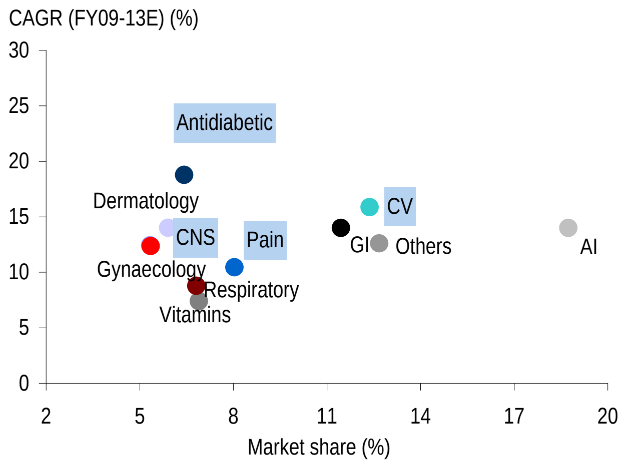
- We recently hosted a *Pharma Investor Day* in Mumbai for institutional clients. Seven pharmaceutical companies participated. The domestic sales-growth story seems to be intact (the industry forecasts rates of about 12-14% YoY over the next three years). Almost all the domestic companies are renewing focus on second-, third- and fourth-tier towns in India. Most companies have increased their domestic sales forces and revised up their sales targets in new therapeutic areas.

Pharaceuticals Sector: domestic market-share breakdown – 2009



Source: Various companies, Daiwa

Pharaceuticals Sector: domestic market-share breakdown – 2013E

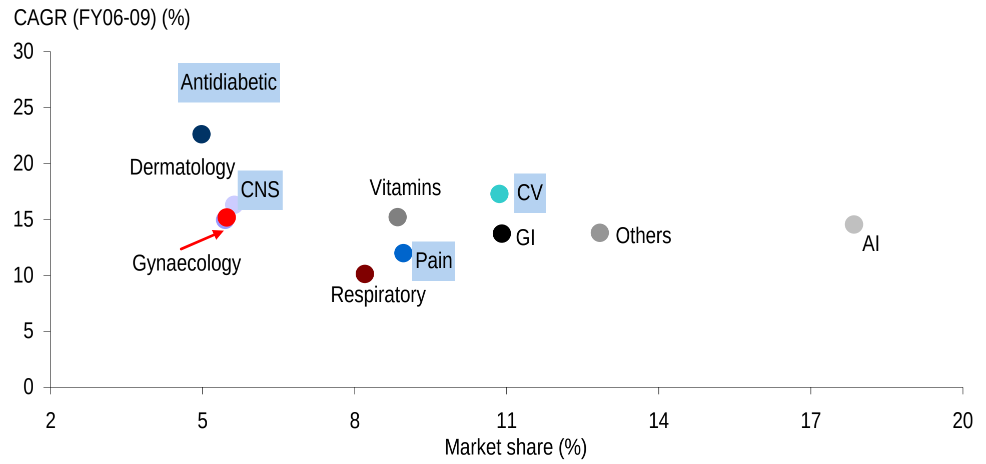


Source: Various companies, Daiwa

- In the contract research and manufacturing services (CRAMS) segment, the sales of the India players over the past three-to-four quarters have been affected by innovators reducing inventory levels. We think there might be one, or at the most two, quarters of inventory de-stocking ahead. High capex is incurred on the back of the fixed long-term contracts signed with innovators. Unlike the generics companies, CRAMS players usually spend on capacity expansion or new plants only when they have long-term contracts with assured sales every year.

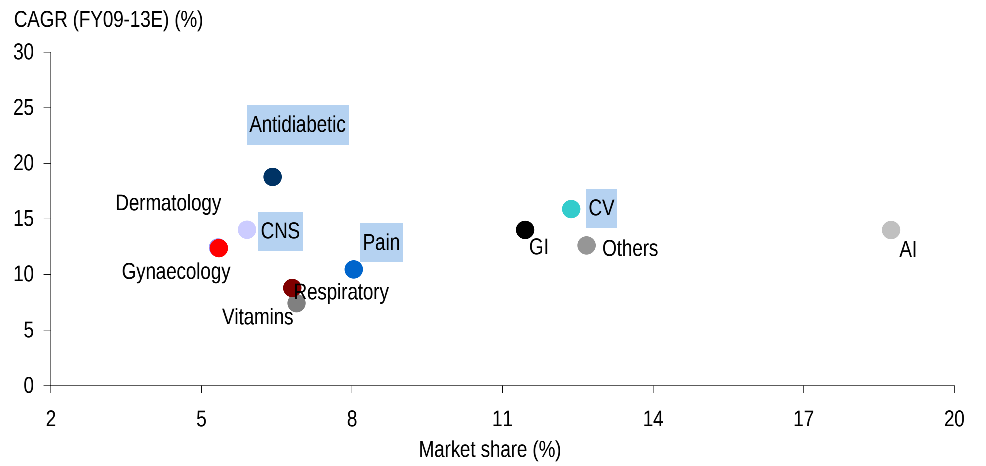
The three most important charts in this report ...

Pharmaceuticals Sector: domestic market-share breakdown – 2009



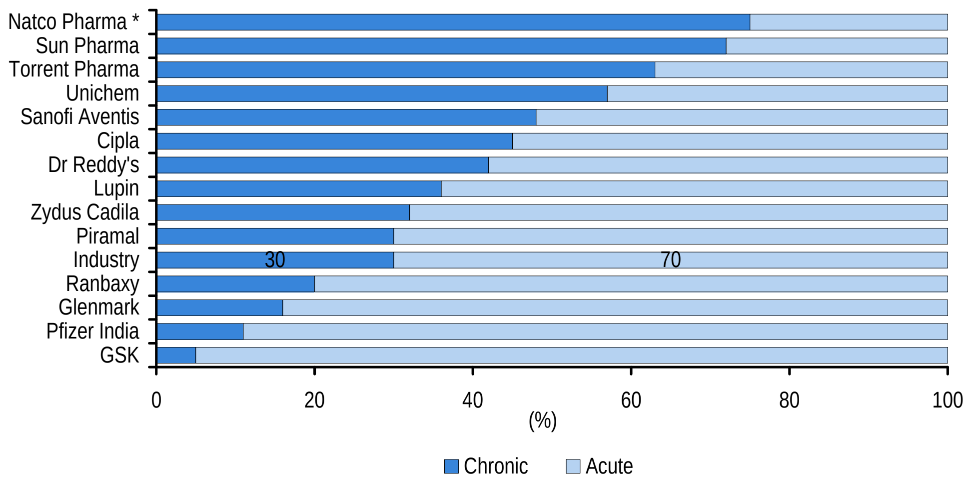
Source: Various companies, Daiwa

Pharmaceuticals Sector: domestic market-share breakdown – 2013E



Source: Various companies, Daiwa

Pharmaceuticals Sector: domestic sales of India companies



Source: compiled by Daiwa
Note: *chronic segment includes oncology drugs prescribed for more than six months

Sun Pharmaceutical Industries – (SUNP IN, Rs1,639.65, 1) six-month target price: Rs1,685

- Sun Pharmaceutical Industries (Sun) continues to rank first in therapies such as psychiatric, neurology, cardiology, orthopaedic and ophthalmology in terms of the number of prescriptions. The company expects domestic sales revenue to increase at a higher rate than for the industry as a whole.
- Spending on R&D as a percentage of sales continues to be about 8%.
- There is limited competition for the generic *Protonix* (*pantaprazole*) based on the price at which the authorised generic drugs sell.
- The company believes that the issues with Caraco issues (related to US federal Drug Administration approval) will take some time to resolve. Some site transfers from Detroit have started, but are not significant.
- Regarding the court case on Taro, Sun is awaiting the response from the Supreme Court of Israel. Taro has yet to restate its most recent audited numbers for 2006 and publish them.
- Sun continues to look for acquisition opportunities. The management will give its guidance on the FY11 prospects after 4Q FY10.

Torrent Pharmaceuticals – (Not rated)

- The breakdown on Torrent Pharmaceutical’s (Torrent) revenue for FY09 was: CRAMS 10%, domestic business 40%, and international operations 50% (Brazil 16%, Russia 4%, Heumann Pharma (Not listed) 16%, Europe 6%, the US 2%, and the rest of the world 6%).
- The company has two manufacturing facilities (in Himachal Pradesh and Gujarat), and plans to set up two more (in Sikkim and Dahej, Gujarat). It plans capex of Rs6bn for the next three-to-four years (with Rs2.5-3bn to be spent on the formulations and the balance on active pharmaceutical ingredients
- The EBITDA margin on the domestic business has been improving. The company is now focusing on second-tier towns, entering new therapy areas, and expanding existing therapies.
- There has been an improvement in the international EBITDA margin for the past three-to-four quarters, due mainly to the improvement in the international operation.
  - Brazil – the market is valued at US$11bn. Torrent has 29% market coverage, and has a sales force of 250 people. The company plans to launch 40 new products by 2013-14; it currently markets 24 products. It expects the ramp-up in sales to increase the EBITDA margin.
  - Mexico – the market is valued at US$10bn. Over the next five years, Torrent plans to launch 34 products, starting with 30-35 people and increasing this to 200.
  - Rest of the world – a total sales force of 263 (Sri Lanka 18%, Vietnam 13%, Africa 14%, the Philippines 19%, Southeast Asia 19%, Australia 5%, others 12%).
  - US – the company currently markets eight products, and has a pipeline of 27 abbreviated new drug applications (ANDA).
  - Heumann Pharma (Germany) – the workforce has been reduced to 66 from 200, and 30% of the total production value has been moved to India.
  - Europe – the company currently has a portfolio of 12 products, and plans to launch 30 that are going off patent.

Dishman Pharmaceuticals & Chemicals – (DISH IN, Rs215.6, 1) six-month target price: Rs252

- Dishman Pharmaceuticals & Chemical (Dishman) had sales of US$230m for FY09. For FY10, the company expects revenue to fall year-on-year due to inventory de-stocking among its customers and a reduction in contract sizes. It expects FY11 and FY12 revenue to rise year-on-year given increased revenue visibility, with larger contracts and as a result of product development.
- Dishman plans to expand four API-manufacturing units, two in FY11 and two in FY12, with annual capex and maintenance capex of Rs1bn of Rs500m, respectively. The annual capex requirements will be met through a mix of internal sources and debt. The company expects commercial production at the new facilities to start in June 2010.
- It expects a near-normal EBITDA margin for FY11. There may be an improvement in the EBITDA margin for FY12, following the new contracts the company expects with various innovators and given full commercial production at the new facilities.
- Dishman expects its net debt of Rs7.9bn as at the end of December 2009 to rise to about Rs8.2bn at the end of FY11. The company is subject to Minimum Alternate Tax, and hence the tax rate will increase to 18% from FY11. However, it expects the credit for export-oriented units to offset the tax increase and lead to an effective tax rate of 10% for FY10 and FY11. This may rise marginally for FY12.
- The current capacity utilisation is about 50%. The company forecasts revenue for the acquired Carbogen Amcis (CA) to decline by about 25% YoY for FY09, and by 5-7% YoY for FY10. The main reason for the declines is budget cuts by clients on R&D. Dishman expects most of the sales growth for FY10 to come from India.

Piramal Healthcare – (PIHC IN, Rs412.8, 1) six-month target price: Rs425

- The domestic business accounts for 50% of total company revenue. The company ranked third in terms of its share of the domestic-formulations market in India for January 2010. It focuses on nine therapeutic areas, including chronic (30%) and acute (70%) segments. It forecasts domestic sales to increase by 15-17% YOY for FY11, higher than the growth rate the industry forecast for itself of 12-14% YOY. Piramal Healthcare (Piramal) expects its sales force to increase by 1,000 every three-to-four years: it is currently the biggest in the industry at 4,000. The company will focus on its existing businesses, and not venture into new therapeutic areas. However, at some time in the future it may look at entering the female healthcare segment, and at domestic-brand acquisitions, but it has no plans for large acquisitions.
- Piramal expects CRAMS revenue to total Rs9.5bn for FY10. The company plans to ramp up production at the Ahmedabad and Chennai early-phase manufacturing facilities and sell the UK plant, which it forecasts to increase the EBITDA margin by about 6% for FY11. The contract with Pfizer (PFE US, US$17.35, 3) has been renewed.
- In the inhalation-anaesthetics market, Piramal expects to account for a 15% share of the addressable US market by the end of FY10.
- Pathology and diagnostics: Piramal expects organic revenue growth of 18% YoY over the next one-to-two years, but to account for only 5% of consolidated revenue. Piramal is collaborating with a Japan blood-glucometer manufacturer to market the latter's products in India. Piramal primarily operates in pathology and radiology labs in first-tier cities in India.

- The company has passed an enabling resolution for a proposal to raise Rs10bn. There is no intention or requirement to conduct the fund-raising exercise in the near future. As at the end of 3Q FY10, Piramal had long-term debt of Rs6.8bn, comprising a mix of foreign and domestic loans, and short-term debt of about Rs5bn, primarily a working-capital loan.

Unichem Laboratories – (Not rated)

- Unichem Laboratories (Unichem) is India's 25th-largest formulations company (in terms of overall prescription generation, with a market share of 1.5%) About 75% of its revenue comes from the domestic market, with 88% of its products not covered by price controls. It has a workforce of about 1,600 people and expects to add 700 over the next two years.

- The company expects sales to rise on the back of investments in its brands, and plans to increase the market share of the 18 brands it has currently. Unichem is looking at entering new segments – women's healthcare, hospitals, OTC and nutrition, biologicals (it has already spent Rs600m on a biotech facility in Goa) – and is increasing its focus on acute therapy. Unichem is shifting its marketing focus from demand-push to demand-pull. The company is focusing on Class III and Class IV cities, and on generating prescriptions and ensuring supply at the retail level. It has strengthened its focus on the BRICS market – including Mexico, Korea, and Turkey.

- It believes new strategies will improve its EBITDA margin.

- The company plans to invest Rs600m (from internal sources) in its facility in Pithampur and an additional Rs800-900m for maintenance.

- The international business accounts for 25% of total revenue.

  - It plans to focus on new products and new markets.

  - It will look at co-production/co-marketing arrangements (it has done this previously with AstraZeneca (Not rated), with cost-sharing clauses and production contracts of about five years.

  - Unichem hopes to reap the benefit of its investment in Niche Generics, UK (acquired in 2002). The company expects it to break even this year and start generating revenue from FY11.

    - It shifted a manufacturing facility to India from Ireland.

    - It retained a packaging facility in Ireland because of the approvals obtained by the facility.

  - The company plans to shift its focus from the UK, and explore the Turkey and Brazil markets (it is working on eight new products currently).

  - It has filed 15 ANDAs, seven of which have been approved so far (and expects to file 25 ANDA over the next two years).

Natco Pharma – (Not rated)

- Revenue for FY09 amounted to Rs4.38bn.
  - The company entered the oncology segment in 2003 and manufactured products at one-tenth of the cost of the innovators. It expects this segment to continue to be a key driver of future sales and earnings growth. Natco Pharma (Natco) expects strong revenue growth from its oncology division over the next two-to-three years. The FY09 revenue for the division was Rs970m.
  - The company moved into the API segment in 1994, and it currently accounts for Rs1bn of revenue, with exports, mainly to Europe, accounting for about 95% of the total.
- Natco has signed a contract for a basket of five drugs with an India company. The products under this collaboration include oral- and injectable-innovator products that are currently on the market. One of the products is *paclitaxel*, which is a generic version of *Abraxane*.
- Natflu (for swine flu) has been launched.

Suven Life Sciences – (Not rated)

- Suven LifeSciences (Suven) continues to focus on the CRAMS space, which accounted for 80% of the total revenue for FY09.
- The outsourcing business is still facing pricing pressure. Suven believes the next five years will be very tough for innovations, because pharmaceuticals companies are reducing their spending on R&D programmes and are even scaling down R&D programmes in the final stages.
- *SUVN 502* (for Alzheimer's/schizophrenia) is entering Phase IIa and two other new chemical entities are at the pre-clinical stage.
- Suven has 35 product patents and 10 process patents.
- The company has started in-house R&D programmes and has 13 molecules in the pipeline.

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