

Biocon**Rs463**
OUTPERFORMER**Event update****Mkt Cap: Rs46.3bn; US\$989mn****Analyst: Nitin Agarwal (91-22-5638 3395; nitinagarwal@sski.co.in)**

Biocon's subsidiary Syngene has entered into an agreement with Bristol-Myers Squib (BMS) for providing R&D services for drug discovery and early drug development. As part of this partnering deal, Syngene will establish a dedicated facility for BMS with almost 400 scientists. This deal will significantly ramp-up Syngene's manpower base and lead to accelerated growth in business over the next few years. Given the high profitability in contract research this deal is positive for Biocon's consolidated earnings growth. In a vindication of our positive view, Biocon's business model has grown from strength to strength over the last few quarters despite near term challenges. While statins business continues to be a challenge, there are multiple positives in form of strong licensing income stream, steady growth of insulin franchise, launch of EPO and a strong nephrology portfolio and imminent launch of GCSF. In recognition of these positives, the stock has got rerated and has been the top performer in SSKI pharma universe over last 6 months. We maintain our Outperformer call with a price target of Rs540 (22x FY08E and 18x FY09E). Increased visibility on the progress of Biocon's discovery projects and Insulin launch schedule in regulated markets will be triggers for upsides.

EVENT: SYNGENE (BIOCON SUBSIDIARY) ENTERS INTO A PARTNERSHIP WITH BMS

Syngene (Biocon's subsidiary involved in contract research) has entered into a research partnership with BMS. As part of this arrangement, Syngene will provide R&D services for discovery and early drug development. BMS benefits by accessing the low cost high quality Indian scientific manpower as well as by expanding the scope of its early stage drug discovery programme and improving its productivity.

□ Very positive development for Syngene

As part of the agreement, Syngene will significantly broaden the scope of its relationship with BMS and undertake a much larger set of activities in area of medicinal chemistry, biology and drug development. Syngene will set up a dedicated research facility for BMS which will scale upto 400 scientists over the next 1-2 years.

This deal clearly underlines Syngene's capabilities in contract research arena and will further strengthen its position as strong player in the global contract research space. While considerably larger in scale, this deal is similar to the deal Wyeth signed in 2006 with GVK Biosciences wherein GVK set up a dedicated research facility for Wyeth.

□ Will accelerate contract research revenue growth for Biocon

Given that Syngene currently has around 600 people on its rolls with 9mFY07 sales of Rs900m, the BMS deal will significantly enhance the scale of its operations and lead to accelerated growth over the next 1-2 years.

We believe that this deal is also likely to generate additional revenue opportunities for other Biocon businesses like Clinigene, the kilo lab facility in Syngene etc. This will lead to additional revenue upsides for Biocon.

We expect the deal to start contributing to revenues from FY08 with significant ramp-up in FY09. Given that contract research has high profitability (40-45% margins), this development is positive for overall profitability growth at Biocon with significant possibilities for upsides given a sharper ramp-up.

We are upgrading our FY08 and FY09 earning estimates by 1.7% and 5% respectively.

❑ CRAMS space – Action is picking up

We have been very positive on the CRAMS story for Indian pharma industry given the profitability pressures faced by global pharma majors and this deal is yet another vindication of our view. Over the last few quarters there has been a continuous stream of developments in the CRAMS space e.g. Suven's partnership deal with Eli Lilly, GVK Biosciences' deal with Wyeth, Advinus' deal with Merck, NPIL's deal with Eli Lilly etc.

We expect regular news flow in CRAMS space going forward and believe that Indian CRAMS companies with strong relationships with innovators will benefit from this trend.

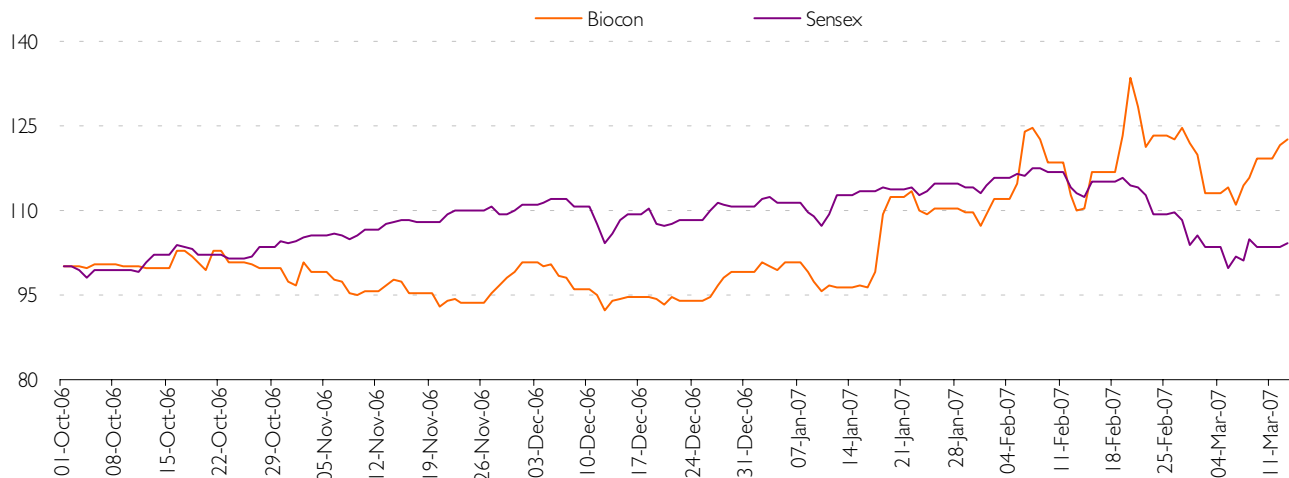
❑ Valuations and view

This BMS deal coupled with launch of nephrology portfolio and strong quarterly performances vindicate our positive view on Biocon's business model despite challenges in the near term. With near stabilization in the fixed cost base, we believe Biocon's improving revenue momentum will start getting reflected into improved operating leverage in subsequent quarters. Expected growth in licensing income with gradual leveraging of Biocon's discovery R&D assets will further aid profitability improvements going forward. We remain excited about the potential for Biocon's insulin business and its discovery pipeline including the Monoclonal Antibody franchise. Biocon is one of the leading Indian players in the lucrative Biogenerics space and will be a strong beneficiary of the improving regulatory environment for launch of these drugs in regulated markets. We maintain our Outperformer call with a price target of Rs540 (22x FY08E and 18x FY09E). Increased visibility on the progress of Biocon's discovery projects and Insulin launch schedule in regulated markets will be triggers for upsides.

Key ratios

Year to March 31	FY05	FY06	FY07E	FY08E	FY09E
Net Profit	1,988	1,743	1,849	2,487	3,207
Shares in issue (m)	100	100	100	100	100
Adj. EPS (Rs)	19.9	17.4	18.5	24.9	32.1
% growth	43.3	(12.3)	6.1	34.5	28.9
PER (x)	23.3	26.6	25.0	18.6	14.4
Price/Book (x)	6.2	5.2	4.4	3.7	3.0
EV/EBITDA (x)	21.2	20.7	17.2	12.9	9.9
ROE (%)	30.5	21.3	19.1	21.5	22.8
ROCE (%)	26.0	20.5	17.7	20.6	22.6
EV/CE (x)	5.4	4.4	3.7	3.0	2.4

Price performance



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1. Outperformer: More than 10% to Index
2. Neutral: Within 0-10% to Index
3. Underperformer: Less than 10% to Index

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