Pfizer

STOCK INFO.	BLOOMBERG
BSE Sensex: 10,609	PFIZ IN
	REUTERS CODE
S&P CNX: 3,128	PFIZ BO

Equity Shares (m)	29.8
52-Week Range	1,225/621
1,6,12 Rel. Perf. (%)	-4/-33/-45
M.Cap. (Rs b)	23.1
M.Cap. (US$ b)	0.5

30 June 2006

Neutral

Previous Recommendation: Neutral Rs775

YEAR END	NET SALES (RS M)	PAT (RS M)	EPS (RS)	EPS GROWTH (%)	P/E (X)	P/BV (X)	ROE (%)	ROCE (%)	EV/ SALES	EV/ EBITDA
11/05A	6,161	827	27.7	44.5	28.0	6.1	22.0	36.1	3.4	15.9
11/06E	7,017	1,073	36.0	29.8	21.6	5.4	25.0	39.7	3.0	12.8
11/07E	6,266	1,031	34.6	-3.9	22.4	4.9	21.7	33.9	3.3	13.1

Pfizer's 2QFY06 performance was better than expected with sales growth of 22% and adjusted PAT growth of 66%. Key highlights include

- Overall net sales grew by 22% (~15% on like-to-like basis) to Rs1.7b, primarily driven by 26.7% YoY growth in pharmaceutical sales. However, de-growth in other business segment viz Animal healthcare business (down by 2.4% YoY) and Service income (down by 14% YoY) restricted topline growth. The growth in pharma business was primarily due to the lower base effect of 2QFY05 wherein sales were impacted due to VAT.
- EBITDA margins expanded by 240bp to 24.7% for the quarter, as the company were able to control costs. Higher other income (up by 66% YoY) and lower tax provisioning (at 28.9% of PBT v/s 38.7% in 2QFY05) further boosted adjusted PAT growth by 66% to Rs316m.
- Pfizer Inc (parent) decision to divest its consumer healthcare (CH) business to Johnson and Johnson (J&J) would result in divestment of domestic CH business to J&J. We have lowered our FY07E EPS to Rs34.5 (by 18%) to factor in this divestment.
- Pfizer is expected to achieve double digit top line growth (for continuing business) over the next couple of years along with margin improvement. However, valuations at 21.6xFY06E and 22.4xFY07E (factoring in for divestment of the Consumer Healthcare division) adequately reflect Pfizer's business fundamentals. Maintain **Neutral** with target price of Rs820 (~24x FY07E EPS factoring in for divestment of consumer health business).

QUARTERLY PERFORMANCE (Rs Million)

Y/E NOVEMBER	FY05				FY06				FY05	FY06E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Net Revenues	**1,383**	**1,421**	**1,695**	**1,753**	**1,535**	**1,729**	**1,835**	**1,917**	**6,252**	**7,017**
YoY Change (%)	*-2.4*	*1.2*	*15.3*	*13.8*	*11.0*	*21.7*	*8.3*	*9.4*	*7.2*	*12.2*
Total Expenditure	1,101	1,104	1,235	1,462	1,104	1,302	1,358	1,113	4,929	5,361
EBITDA	**282**	**317**	**461**	**291**	**431**	**426**	**478**	**805**	**1,322**	**1,656**
Margins (%)	*20.4*	*22.3*	*27.2*	*16.6*	*28.1*	*24.7*	*26.0*	*42.0*	*21.2*	*23.6*
Depreciation	29	37	32	40	31	32	36	43	139	142
Other Income	34	31	34	45	45	51	47	33	144	175
PBT before EO Items	**285**	**311**	**462**	**296**	**445**	**445**	**489**	**795**	**1,326**	**1,690**
EO Expense/(Income)	58	58	115	34	58	-60	58	57	234	232
PBT after EO items	**226**	**252**	**347**	**262**	**387**	**505**	**431**	**738**	**1,092**	**1,458**
Tax	92	98	129	88	139	146	157	32	411	474
Rate (%)	*40.5*	*38.7*	*37.2*	*33.7*	*35.9*	*28.9*	*36.5*	*12.2*	*37.6*	*36.5*
Reported PAT	**135**	**155**	**218**	**174**	**248**	**359**	**273**	**648**	**681**	**926**
PAT adj. for Excep Items	**169**	**191**	**291**	**196**	**285**	**316**	**310**	**698**	**827**	**1,073**
YoY Change (%)	*27.0*	*60.0*	*87.4*	*19.8*	*68.3*	*66.1*	*6.8*	*255.4*	*44.5*	*29.8*
Margins (%)	*12.2*	*13.4*	*17.1*	*11.2*	*18.6*	*18.3*	*16.9*	*36.4*	*13.2*	*15.3*

E: MOSt Estimates

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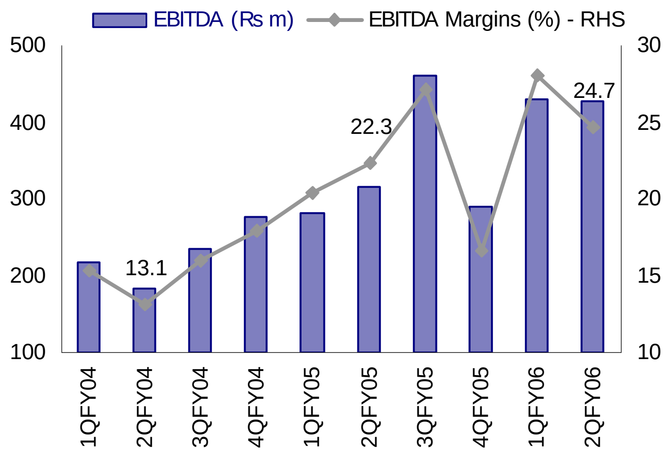
Low base boosts topline growth

Net sales grew by 22% to Rs1.7b, primarily driven by 26.7% YoY growth in pharmaceutical sales. However, de-growth in other business segment viz Animal healthcare business (down by 2.4% YoY) and Service income (down by 14% YoY) restricted topline growth. However, on like-to-like basis, growth would be approximately 15% YoY.

The growth in pharma business was primarily due to the lower base effect of 2QFY05 wherein sales were impacted due to VAT. Also, the three recent launches (Viagra, Lyrica and Caduet) started meaningful contribution (YTD Rs50m) during the quarter. The animal healthcare business degrew mainly due to the impact of the bird-flu.

EBITDA MARGIN TREND



Source: Company/Motilal Oswal Securities

SEGMENT MIX (RS M)

	2QFY06	2QFY05	YOY (%)	1QFY06	QOQ (%)
Pharmaceuticals	1,524	1,202	26.7	1,307	16.6
% of sales	*88.1*	*84.6*		*85.1*	
Animal Health	148	152	-2.4	154	-3.6
% of sales	*8.6*	*10.7*		*10.0*	
Services Income	57	66	-14.3	74	-23.5
% of sales	*3.3*	*4.7*		*4.8*	
Total	**1,729**	**1,421**	**21.7**	**1,535**	**12.6**

Source: Company/Motilal Oswal Securities

The pharma business has witnessed a 220bp decline in PBIT margins to 25.6% in 2QFY06 mainly due to higher cost of purchased goods for recently launched products. However, PBIT margins of the Animal Healthcare business showed a significant improvement at 2.8% (v/s -6.6% in 2QFY05).

PBIT MARGIN (RS M)

	2QFY06	2QFY05	YOY (%)	1QFY06	QOQ (%)
Pharmaceuticals	390	334	16.8	362	7.7
% of sales	*25.6*	*27.8*		*27.7*	
Animal Health	4	-10	-139.0	38	-89.6
% of sales	*2.6*	*-6.6*		*24.4*	
Services-Clinical devlp.	8	6	23.4	8	-1.3
% of sales	*13.9*	*9.6*		*10.8*	
Total	**402**	**331**	**21.6**	**408**	**-1.4**

Source: Company/ Motilal Oswal Securities

Better business mix leads to margin expansion

EBITDA margins during the quarter expanded by 240bp (on a low base) to 24.7% for the quarter, as the company were able to control costs as reflected in other expenditure (at 24.9% of sales v/s 29.6% in 2QFY05).

The company has launched three products (Viagra, Caduet and Lyrica) recently. We believe that the company would have imported these new products from the parent for filling the pipeline, resulting in increase in purchase of finished goods (as reflected in higher RM cost at 37.8% of sales v/s 35.2% in 2QFY05).

Other income and lower tax boost net profit

Higher other income (up by 66% YoY), lower tax provisioning (at 28.9% of PBT v/s 38.7% in 2QFY05) and profit on sale of Hyderabad plant (Rs118m) further boosted reported PAT to Rs359m. However, adjusting for non-recurring items (VRS expense and profit on sale of plant) recurring PAT grew by 66% to Rs316m.

Sale of Consumer Healthcare business: Significant impact on earnings

Pfizer (USA) has decided to divest it consumer healthcare (CH) business to Johnson and Johnson (J&J). As a result of the global sellout of the consumer healthcare business, Pfizer India will also have to divest its domestic consumer healthcare business in favor of J&J. Key products in this portfolio include the Benadryl and Listerine ranges as well as Gelusil. These products enjoy very high brand equity. We expect divestment of domestic CH business to be completed by end of FY06. This division contributed about Rs1.4b (20% of sales) to Pfizer's revenues in FY05. We have lowered our earnings estimate to factor in the divestment of the CH business. The divestment of CH business would result in loss of sales at Rs1.5b and reduction in PAT by Rs230m (EPS of Rs7.7/share) for FY07E. Although, our estimates don't factor in the cashflow accruing from the divestment of this business, however, the company might utilize this cashflow for giving one-time special dividend or buy-back of shares.

CONSUMER HEALTHCARE (CH) BUSINESS - SENSITIVITY ANALYSIS (RS M)

PARTICULARS	2007E
Total Sales	**7,789**
CH Sales	1,532
% of total	*20*
CH NPM (%) – assumed	15
CH PAT	230
Total PAT	**1,255**
% of total	*18*
CH EPS	7.7
EPS post-divestment (Rs)	34.4
P/E post-divestment	22.4

Note - We have assumed that the consideration for sale of CH division will be returned to investors as one-time dividend

Source: Motilal Oswal Securities

Aggressive launches in the recent past

Pfizer has launched three new drugs in the past three quarters in the domestic market. These include Viagra (for erectile dysfunction – Rs800m market), Caduet (combination of Atorvastatin and Amlodipine in the CVS category) and Lyrica (for neuropathic pain – Rs1.0b market). While it is too early to comment on the success of these drugs, we see this as a positive development, as it indicates efforts for mapping the parent's global product portfolio into the domestic entity. Pfizer management has indicated that it is looking at launching more products from the parent's portfolio and will also explore the in-licensing route for new launches. Pfizer Inc's CEO has recently indicated that India and China will be key focus markets in the company's Asia plans.

Pfizer has adopted a premium pricing strategy for these products since they are imported directly from the parent. For e.g. Viagra is priced at about 20x the price of generic versions already launched in the market.

NEW LAUNCHES – PREMIUM PRICING

PRODUCT	RETAIL PRICE (RS)
Viagra (50mg tablet)	463
Viagra (100mg tablet)	594
Lyrica (75mg x 14)	739
Lyrica (150mg x 14)	1108
Caduet (5mg Amlodipine/10mg Atorvastatin)/tab	58
Caduet (5mg Amlodipine/20mg Atorvastatin)/tab	104

Source: Motilal Oswal Securities

But, despite the premium pricing Pfizer has been able to garner 1.8% share for Viagra in the Rs800m erectile dysfunction (ED) market in India. Pfizer is targeting about 10%-15% share for Viagra over the next 2-3 years led by its promotional efforts coupled with the scientific skills available with the parent.

Strong pipeline of the parent should augur well

Pfizer (USA) has among the strongest R&D pipelines amongst global pharmaceutical companies. The parent has a pipeline of more than 150 new molecules at various stages of development. It is targeting about 5 NDA filings with the US FDA over CY06-CY07. Some of these products could be launched in India with a time lag.

R&D PIPELINE	
New molecules in R&D Pipeline	152
New improvements over existing drugs	83
Total NCEs	**235**

PFIZER (USA) – LAUNCHES PLANNED IN 2006

DRUG	THERAPEUTIC SEGMENT	PATENT EXPIRY	POST-1995 DRUG	IPR STATUS IN INDIA
Exubera	Inhaled Insulin for diabetics	2014	Unlikely	Despite being a pre-1995 drug, Exubera is likely to enjoy an indirect monopoly since it is the only inhaled Insulin developed globally till date. Patients will have to trade-off between premium pricing and dosage convenience. Global launch is targeted in 2006 and we expect India launch towards end of 2007
Sutent	Anti-cancer	2021	Yes	Likely to enjoy patent protection in India but can be launched through 100% subsidiary
Champix	Smoking cessation	N.A.	N.A.	Currently under US FDA priority review. May not have a big market in India since such drugs have failed in the past
Indiplon	Insomnia	N.A.	N.A.	
Eraxis	Anti-fungal	N.A.	N.A.	
Zeven	Anti-biotic	N.A.	N.A.	

Source: Pfizer (USA), Motilal Oswal Securities

FILINGS WITH US FDA

Filings Pending Approval	6	
Filings targeted in 2006	2	Maraviroc (anti-AIDS) & an in-licensed drug. Likely to enjoy patent protection in India
Filings targeted in 2007	3	Torcetrapib/Atorvastatin combination, Asenapine (Schizophrenia) & an anti-cancer drug. Last two drugs may enjoy patent protection in India. Cancer drug may be launched through 100% subsidiary

Source: Pfizer (USA)/ Motilal Oswal Securities

Pfizer (USA) is also targeting about six new launches globally which are likely to be launched in India, again with a time lag. The table below indicates the details on these drugs and their likely IPR status in India.

Patent regime will result in long term upsides

We believe that the patent regime will flag off significant benefits for Pfizer, albeit in the long term. We expect launch of patented products from the parent's portfolio by 2008. Although clarity on this will emerge only by 2007, we present below the potential upside to Pfizer from the patent regime.

POTENTIAL UPSIDE EXPECTED FROM LAUNCH OF PATENTS IN 2008 (RS M)

	CY08	CY09	CY10	CY11	CY12	CY13	CY14	CY15
No. of Patented Products Launched - Assumed	1	2	2	2	2	1	1	1
Total no. of Patented Products on Market	**1**	**3**	**5**	**7**	**9**	**10**	**11**	**12**
Sales								
Product A	300	600	1,250	1,500	1,800	1,980	2,178	2,396
Product B	0	300	600	1,250	1,500	1,800	1,980	2,178
Product C	0	300	600	1,250	1,500	1,800	1,980	2,178
Product D	0	0	300	600	1,250	1,500	1,800	1,980
Product E	0	0	300	600	1,250	1,500	1,800	1,980
Product F	0	0	0	300	600	1,250	1,500	1,800
Product G	0	0	0	300	600	1,250	1,500	1,800
Product H	0	0	0	0	300	600	1,250	1,500
Product I	0	0	0	0	300	600	1,250	1,500
Product J	0	0	0	0	0	300	600	1,250
Product K	0	0	0	0	0	0	300	600
Product L	0	0	0	0	0	0	0	300
Total Sales	**300**	**1,200**	**3,050**	**5,800**	**9,100**	**12,580**	**16,138**	**19,462**
NPM (%) – Assumed	20	20	20	20	20	20	20	20
Net Profit	60	240	610	1,160	1,820	2,516	3,228	3,892
Incremental EPS (Rs)	2	8	20	39	61	84	108	130
P/E for Patented Products (x)	40	40	40	40	40	40	40	40
Valuation for Patented Products (Rs/sh.)	80	322	818	1,555	2,440	3,373	4,327	5,218

Source: Company/ Motilal Oswal Securities

Valuations reflect positives; lowering target price to Rs820

Pfizer is now firmly on the path of margin improvement, with improved efficiencies and control on costs expected to drive rapid improvement in margins. The company has gone through a couple of value dilutive mergers (with Parke Davis and Pharmacia) in the past, which took a severe toll on margins in the past. However, things are back on track and the LEAP program alone is expected to lead to 930bp higher EBIDTA margins over FY04-FY06E. With revenues expected to grow at double digit (for continuing business), we expect EBIDTA margins to trend upward by 350bp to 24.9% in the FY05-FY07E period. We have assumed lower EBITDA margins for FY07E to take into account the pre-launch promotional expenditure that the company is likely to incur for its patented products (expected to be launched in 2008).

In our opinion, Pfizer is likely to achieve double digit growth over the next couple of years in revenues along with improvement in margins on the back of the LEAP program. However valuations of 21.6xFY06E and 22.4xFY07E (post divestment of CH division), adequately reflect the business fundamentals. We are lowering our price target by 18% to Rs820 (~24x FY07E EPS) to factor in divestment of consumer healthcare business. Maintain **Neutral.**

Pfizer: an investment profile

Company description

Pfizer India, a 40% subsidiary of Pfizer Inc, has interests in pharmaceutical business (~86% of sales), animal health (~10% of sales) and services (~4% of sales). Pfizer India's profile is completely different from its parent and many other emerging market subsidiaries. Pfizer has a strong field force; however these are skewed towards mature categories owing to the nature of its product portfolio.

Key investment arguments

- With merger integration related issues out of the way, Pfizer has started focusing on gearing up for the product patent era
- Focus on revamping the sales force in line with the parent's focus therapeutic areas
- Over the longer term, Pfizer with its parent's robust pipeline and strong brand equity in India could emerge as a key gainer from product patent introduction

Key investment risks

- Has a 100% subsidiary in India through which some of the patented products could be launched in the coming years.
- Ineffective implementation of product patents in India could suppress growth potential

Recent developments

- Divestment of consumer healthcare business by Pfizer Inc would result in divestment of domestic consumer healthcare business.

Valuation and view

- Valuations of 21.6x and 22.4x FY06E and FY07E earnings respectively fairly discount the rapid growth prospects and rich pipeline of the parent
- Re-iterate **Neutral**, with a target price of Rs820.

Sector view

- Indian Pharma market expected to witness steady growth, on the back of gradual increase in the low penetration levels – companies with strong brands and marketing muscle to benefit the most
- IPR regime unlikely to lead to any major change in the near term; MNCs and large Indian players to benefit over the longer term.
- Among MNCs, we are bullish on companies whose domestic portfolio is well aligned with its parent and where risk of conflict with 100% subsidiaries is limited

COMPARATIVE VALUATIONS

		PFIZER	AVENTIS	GLAXO
P/E (x)	FY07E	21.6	18.6	22.8
	FY08E	22.4	17.8	22.3
P/BV (x)	FY07E	5.4	5.3	7.5
	FY08E	4.9	4.5	6.2
EV/Sales (x)	FY07E	3.0	3.2	4.6
	FY08E	3.3	2.8	4.4
EV/EBITDA (x)	FY07E	12.8	11.3	14.8
	FY08E	13.1	10.4	14.4

SHAREHOLDING PATTERN (%)

	MAR.06	DEC.05	MAR.05
Promoters	41.2	41.2	40.0
Domestic Institutions	26.5	26.1	28.0
FIIs/FDIs	6.0	6.6	5.3
Others	26.4	26.0	26.8

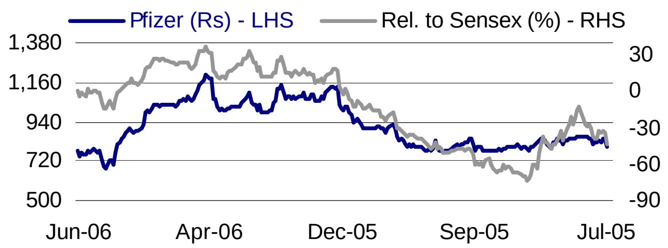
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY06	36.0	34.2	5.2
FY07	34.6	40.1	-13.6

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
775	820	5.8	Neutral

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT					(Rs Million)
Y/E NOVEMBER	2003	2004^	2005^	2006E^	2007E^
Net Income	**5,041**	**5,820**	**6,161**	**7,017**	**6,266**
Change (%)	*-14.0*	*15.5*	*5.8*	*13.9*	*-10.7*
Total Expenditure	4,409	4,910	4,838	5,361	4,704
EBITDA	**632**	**911**	**1,322**	**1,656**	**1,562**
Change (%)	*-40.7*	*44.1*	*45.2*	*25.2*	*-5.7*
Margin (%)	*12.5*	*15.6*	*21.5*	*23.6*	*24.9*
Depreciation	108	103	138	142	146
Int. and Finance Charges	4	8	2	0	0
Other Income - Rec.	111	141	144	175	208
PBT & EO Items	**630**	**941**	**1,326**	**1,690**	**1,624**
Change (%)	*-43.5*	*49.2*	*41.0*	*27.4*	*-3.9*
Extra Ordinary Items	-167	-192	-234	-232	-135
PBT after EO Items	**463**	**748**	**1092**	**1458**	**1489**
Tax	188	293	411	532	543
Tax Rate (%)	*40.6*	*39.2*	*37.6*	*36.5*	*36.5*
Reported PAT	**275**	**455**	**681**	**926**	**945**
PAT Adj for EO Items	**374**	**572**	**827**	**1,073**	**1,031**
Change (%)	*-44.0*	*52.8*	*44.5*	*29.8*	*-3.9*
Margin (%)	7.4	9.8	13.4	15.3	16.5

^2004, 2005E and 2006E include the merger effect of Pharmacia

BALANCE SHEET					(Rs Million)
Y/E NOVEMBER	2003	2004^	2005^	2006E^	2007E^
Equity Share Capital	288	298	298	298	298
Reserves	2,796	3,129	3,467	3,993	4,461
Net Worth	**3,084**	**3,428**	**3,766**	**4,291**	**4,759**
Loans	0	120	0	0	0
Deferred Tax Liabilities	-99	-64	-90	-32	28
Capital Employed	**2,985**	**3,484**	**3,675**	**4,259**	**4,787**
Gross Block	1,368	1,588	1,701	1,988	2,188
Less: Accum. Deprn.	802	871	946	1,088	1,234
Net Fixed Assets	**566**	**717**	**756**	**900**	**954**
Capital WIP	45	39	21	30	30
Investments	32	32	0	0	0
Curr. Assets	**3,182**	**3,772**	**4,516**	**5,114**	**5,593**
Inventory	866	739	898	1,179	1,053
Account Receivables	588	717	828	961	858
Cash and Bank Balance	891	1,611	2,099	1,922	2,742
Others	837	705	691	1,053	940
Curr. Liability & Prov.	**1,381**	**1,677**	**1,985**	**2,119**	**2,041**
Account Payables	962	1,135	1,340	1,403	1,253
Provisions	419	542	645	716	787
Net Current Assets	**1,801**	**2,094**	**2,531**	**2,995**	**3,553**
Deferred Revenue Exp (VRS)	540	601	367	333	250
Appl. of Funds	**2,985**	**3,484**	**3,675**	**4,259**	**4,787**

E: MOSt Estimates

RATIOS					
Y/E NOVEMBER	2003	2004	2005^	2006E	2007E
Basic (Rs)					
EPS	**13.0**	**19.2**	**27.7**	**36.0**	**34.6**
Cash EPS	16.8	22.6	32.4	40.7	39.4
BV/Share	107.1	114.9	126.2	143.8	159.5
DPS	7.5	10.0	10.0	11.8	14.0
Payout (%)	88.6	71.8	50.4	43.3	50.5
Valuation (x)					
P/E		40.4	28.0	21.6	22.4
Cash P/E		34.3	24.0	19.0	19.7
P/BV		6.8	6.1	5.4	4.9
EV/Sales		3.7	3.4	3.0	3.3
EV/EBITDA		23.8	15.9	12.8	13.1
Dividend Yield (%)		1.3	1.3	1.5	1.8
Return Ratios (%)					
RoE	12.1	16.7	22.0	25.0	21.7
RoCE	21.3	27.2	36.1	39.7	33.9
Working Capital Ratios					
Asset Turnover (x)	1.7	1.7	1.7	1.6	1.3
Debtor (Days)	43	45	49	50	50
Inventory (Days)	63	46	53	61	61
Working Capital (Days)	66	30	26	56	47
Leverage Ratio					
Current ratio	2.3	2.2	2.3	2.4	2.7
Debt/Equity	0.0	0.0	0.0	0.0	0.0

CASH FLOW STATEMENT					(Rs Million)
Y/E NOVEMBER	2003	2004^	2005^	2006E	2007E
Oper. Profit/(Loss) before Tax	613	850	1,556	1,690	1,645
Interest/Dividends Recd.	111	141	144	175	208
Direct Taxes Paid	-208	-258	-438	-474	-484
(Inc)/Dec in WC	262	427	51	-642	263
CF from Operations	**779**	**1,160**	**1,313**	**750**	**1,632**
EO Items	-167	-192	-234	-232	-135
CF from Opr.incl EO Item	**611**	**968**	**1,080**	**518**	**1,497**
(Inc)/Dec in FA	-150	-248	-159	-295	-200
(Pur)/Sale of Investments	20	0	32	0	0
CF from Investments	**-129**	**-248**	**-127**	**-295**	**-200**
Issue of Shares	0	10	0	0	0
Inc/(Dec) in Debt	0	120	-120	0	0
Dividend Paid	-244	-327	-343	-400	-477
Interest paid	-4	-8	-2	0	0
Others	-28	205	0	0	0
CF from Fin. Activity	**-275**	**0**	**-465**	**-400**	**-477**
Inc/Dec of Cash	**207**	**720**	**488**	**-177**	**821**
Add: Beginning Balance	684	891	1,611	2,099	1,922
Closing Balance	**891**	**1,611**	**2,099**	**1,922**	**2,742**

^ 2004 and 2003 balance sheet items are not comparable due to Pharmacia merger

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Disclosure of Interest Statement	**Pfizer**
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	Yes
3. Broking relationship with company covered	No
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