

Healthcare
 Pharmaceuticals
 Equity – India

Neutral

Target price (INR)	500.00
Share price (INR)	444.10
Forecast dividend yield (%)	0.9
Potential return (%)	13.5

Note: Potential return equals the percentage difference between the current share price and the target price, plus the forecast dividend yield

Performance	1M	3M	12M
Absolute (%)	-13.4	-8.0	-24.1
Relative ^A (%)	-4.9	-4.8	-8.1

Index^A BOMBAY SE IDX

RIC RANB.BO
 Bloomberg RBXY IN

Market cap (USDm) 3,509
 Market cap (INRm) 183,208

Enterprise value (INRm) 198614
 Free float (%) 36

Note: (V) = volatile (please see disclosure appendix)

1 December 2011

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Ranbaxy

Downgrade to N: RBXY plays Teva card to end gLipitor woes

- ▶ **Ranbaxy announces launch of gLipitor (atorvastatin) in the US from NJ facility – this is the largest US generic launch**
- ▶ **Timely launch positive, though tie-up with Teva dents upside potential, possible c30-33% profit sharing arrangement**
- ▶ **Downgrade to N from OW, given near-term catalyst played out; Mohali facility FDA approval and India ramp-up to aid in slow base recovery; cut TP to INR500 from INR565**

Finally positive verdict on Lipitor: Ranbaxy announced the launch of generic Lipitor (atorvastatin calcium) in the US, in all strengths, from Ohms Laboratories, a facility in New Jersey. This is in line with our expectation of a timely launch and should bring significant gains in next six months. Watson has also an authorised generic and has launched the product as well.

Focus shifts to market share gain and pricing: Watson has indicated that it has launched with a 50% discount to the branded drug's retail price. Pfizer has been working on a strategy to extend the life of the branded drug by offering to sell branded Lipitor directly to payors (pharmacies and insurance companies) at lower prices. While such strategies are not new to innovator companies, given Pfizer's aggressiveness to protect brand share, we are cautious on Ranbaxy's market share gains. Our current valuation assumes a c40% share for Ranbaxy, with c65% price erosion.

Partnership with Teva – an unknown: Ranbaxy's tie-up with Teva, while not a major surprise, is a setback to sentiment. We believe Ranbaxy would have kept Teva as a back-up plan in case manufacturing issues prevented the approval of the product. Although terms of the agreement are not disclosed, based on an incremental USD0.10 EPS impact as per Teva from an unknown drug in 4Q11, we assume Ranbaxy will share cUSD90-100m in profits (c30% share of the total profit from the opportunity).

Downgrade to N from OW as an important catalyst played out: With the Lipitor catalyst playing out, we believe there are few near-term catalysts. The next important launches are expected to be gProvigil in April 2012 and gActos in August 2012. We are cutting our estimates, factoring in a lower profit contribution post-Teva. We value RBXY at 20x September 2013e EPS of INR22.2 and add a reduced para-IV value of INR53, down from earlier INR70, on account of the profit sharing agreement with Teva for generic Lipitor. Upside risks include the clearance of facilities and the resolution of AIP, though we believe this could further test investor's patience. Downside risks are the difficulty in gaining market share and a higher-than-assumed price erosion in gLipitor during period of exclusivity (180 days) and in the period beyond May 2012.

Financials & valuation

Financial statements

Year to	12/2010a	12/2011e	12/2012e	12/2013e
Profit & loss summary (INRm)				
Revenue	85,494	102,642	107,921	114,284
EBITDA	15,351	25,239	25,645	26,637
Depreciation & amortisation	-5,533	-3,059	-3,500	-3,800
Operating profit/EBIT	9,818	22,180	22,145	22,837
Net interest	972	-644	-650	-500
PBT	16,896	19,639	25,145	26,537
HSBC PBT	16,896	19,639	25,145	26,537
Taxation	-5,849	-5,204	-6,035	-6,369
Net profit	10,862	14,268	18,960	19,983
HSBC net profit	2,834	6,607	8,733	9,756

Cash flow summary (INRm)

Year to	12/2010a	12/2011e	12/2012e	12/2013e
Cash flow from operations	10,248	3,405	16,778	28,872
Capex	-3,694	-4,000	-3,500	-3,000
Cash flow from investment	-331	-467	-3,464	-2,500
Dividends	-982	-1,817	-2,401	-2,683
Change in net debt	-12,752	8,981	-13,453	-26,407
FCF equity	448	1,303	9,628	21,672

Balance sheet summary (INRm)

Year to	12/2010a	12/2011e	12/2012e	12/2013e
Intangible fixed assets	27,946	27,946	27,946	27,946
Tangible fixed assets	21,350	22,292	22,292	21,492
Current assets	91,916	72,068	94,921	114,539
Cash & others	37,629	13,606	25,060	49,467
Total assets	141,213	122,306	145,158	163,977
Operating liabilities	41,398	31,485	37,052	37,166
Gross debt	43,348	28,306	26,306	24,306
Net debt	5,719	14,700	1,247	-25,161
Shareholders funds	55,981	61,963	80,213	99,417
Invested capital	62,186	77,215	83,047	77,344

Ratio, growth and per share analysis

Year to	12/2010a	12/2011e	12/2012e	12/2013e
Y-o-y % change				
Revenue	13.4	20.1	5.1	5.9
EBITDA	115.9	64.4	1.6	3.9
Operating profit	121.5	125.9	-0.2	3.1
PBT	67.3	16.2	28.0	5.5
HSBC EPS	726.4	133.1	32.2	11.7

Ratios (%)

Year to	12/2010a	12/2011e	12/2012e	12/2013e
Revenue/IC (x)	1.4	1.5	1.3	1.4
ROIC	10.2	23.7	21.3	21.9
ROE	5.8	11.2	12.3	10.9
ROA	8.1	11.3	14.7	13.3
EBITDA margin	18.0	24.6	23.8	23.3
Operating profit margin	11.5	21.6	20.5	20.0
EBITDA/net interest (x)		39.2	39.5	53.3
Net debt/equity	10.1	23.5	1.5	-25.2
Net debt/EBITDA (x)	0.4	0.6	0.0	-0.9
CF from operations/net debt	179.2	23.2	1345.9	

Per share data (INR)

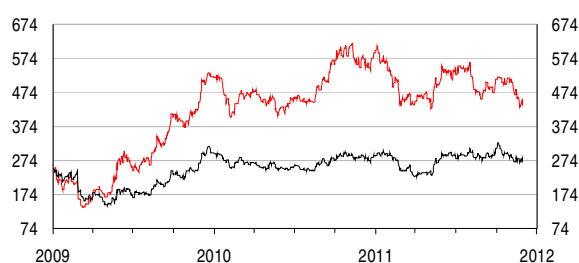
Year to	12/2010a	12/2011e	12/2012e	12/2013e
EPS reported (fully diluted)	25.38	33.35	44.31	46.70
HSBC EPS (fully diluted)	6.62	15.44	20.41	22.80
DPS	1.97	3.86	5.10	5.70
Book value	130.83	144.81	187.46	232.34

Valuation data

Year to	12/2010a	12/2011e	12/2012e	12/2013e
EV/sales	2.2	1.9	1.7	1.4
EV/EBITDA	12.4	7.9	7.2	5.9
EV/IC	3.0	2.6	2.2	2.0
PE*	65.6	28.1	21.3	19.1
P/Book value	3.3	3.0	2.3	1.9
FCF yield (%)	0.2	0.7	5.2	11.8
Dividend yield (%)	0.5	0.9	1.2	1.3

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Source: HSBC

Note: price at close of 30 Nov 2011

Valuation and risks

We continue to value the base business at 20x September 2013e EPS, maintaining a 10% premium to the sector average. Our PE multiple is in line with other large caps (at 10% to the sector average) on account for the company's large exclusive generic opportunities in the US, including atorvastatin, modafinil, esomeprazole, pioglitazone, and valsartan. We reduce the para-IV opportunity value to INR53 from INR70 on account of the profit sharing agreement with Teva for generic Lipitor. Our target price of INR500 presents c13.7% potential return from current levels.

Under our research model, for stocks without a volatility indicator, the Neutral band is 5 percentage points above and below the hurdle rate for Indian stocks of 11.0%. Our new target price of INR500 implies a potential return of 13.7%, within the Neutral band; therefore, we are downgrading our Overweight rating to Neutral. Potential return equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated.

Risks: The key upside risk is the resolution of the affected Paonta and Dewas facilities, though the potential upside will likely be offset by the payment of fines. The downside risks are the difficulty in gaining market share and a higher-than-assumed price erosion in gLipitor during period of exclusivity (180 days) and in the period beyond May 2012.

Key generic launches in US – expected timeline

	Molecule	Brand	Indication	Sales (USDm)	Who is FTF?	Timeline
1	Levofloxacin	Levaquin	Quinolone Anti-Infective	1,312	Multiple	Launched
2	Atorvastatin	Lipitor	High Cholesterol	5,329	Ranbaxy	Launched
3	Atorvastatin, amlodipine	Caduet	High Cholesterol And High BP	800	Ranbaxy	Delayed
4	Minocycline	Solodyn	Acne	370	Impax, Teva, Sandoz, Mylan, Ranbaxy	Expected immediate
5	Alfuzosin	Uroxatral	Benign Prostatic Hyperplasia	200	Multiple	FY12
6	Irbesartan/hctz	Avalide/Avapro	Hypertension & CHF		Teva/ Ranbaxy?	Mar-12
7	Modafinil	Provigil	Narcolepsy	961	Ranbaxy, Teva, Mylan	Apr-12
8	Desloratadine	Clarinx	Anti-Histamine	249	Multiple	Jul-12
9	Pioglitazone	Actos	Type-2 Diabetes	3,212	Ranbaxy, Mylan, Watson	Aug-12
10	Valsartan	Diovan	Hypertension & CHF	2,520	Ranbaxy	Sep-12
11	Fenofibrate	TriCor	High Cholesterol	1,578	Teva	Oct-12
12	Valganciclovir	Valcyte	Cytomegalovirus Infections	400	Ranbaxy	Mar-13
13	Oxycodone	Oxycontin	Moderate To Severe Pain	3,150	Ranbaxy, Teva, Endo	Apr-13
14	Pioglitazone + metformin	Actoplus met	Type-2 Diabetes	478	Mylan	Jun-13
15	Rivastigmine	Exelon solution	Alzheimer's Disease	<5	Ranbaxy?	Feb-14
16	Esomeprazole	Nexium	GERD	2,695	Ranbaxy	May-14
17	Memantine	Namenda	Alzheimer's Disease	600	Multiple	Jan-15
18	Fenofibrate	Antara	Hypercholesterolemia	60	Dr Reddys	Unknown
	Total			22,542		

Source: HSBC estimates

Disclosure appendix

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Neutral (Hold)	35%	(22% of these provided with Investment Banking Services)
Underweight (Sell)	11%	(13% of these provided with Investment Banking Services)

Share price and rating changes for long-term investment opportunities

Ranbaxy (RANB.BO) Share Price performance INR Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
N/A	Overweight	20 January 2011
Target Price	Value	Date
Price 1	690.00	20 January 2011
Price 2	565.00	10 May 2011

Source: HSBC

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Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
RANBAXY	RANB.NS	434.65	30-Nov-2011	2, 4, 7

Source: HSBC

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