

Healthcare  
 Pharmaceuticals  
 Equity – India

## Overweight

Target price (INR)	930.00
Share price (INR)	710.40
Forecast dividend yield (%)	1.0
Potential return (%)	31.9

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 (%)	-0.7	-13.8	-9.7
Relative <sup>A</sup> (%)	7.1	-2.8	18.4

Index<sup>A</sup> BOMBAY SE SENSITIVE INDEX

RIC	CADI.BO
Bloomberg	CDH IN
Market cap (USDm)	2,750
Market cap (INRm)	145,453
Enterprise value (INRm)	152,870
Free float (%)	25

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# Cadila Healthcare (CDH IN)

OW: Cadila strengthens domestic portfolio with Biochem

- ▶ **Cadila acquires privately held Biochem Pharma for an undisclosed sum, its third acquisition in FY12 after Neshor and Bremer Pharma**
- ▶ **Biochem is primarily an anti-infectives player (80% of sales) with some presence in cardiac, oncology, anti-diabetic**
- ▶ **We remain OW on the stock on the back of strong ramp up in US sales. Our 12-month TP is INR930 (unchanged)**

**Cadila acquires 100% stake in Biochem Pharmaceuticals**, a privately-held company based in Mumbai for an undisclosed amount. For the year ending March 2011, Biochem reported sales of INR2.65bn with c80% contribution from anti-infectives portfolio. Past acquisitions (Liva healthcare (2007), Brand Aten and German Remedies (2001) and Recon healthcare (2000)) have helped Cadila become one of the top five players in India.

**Biochem's top five brands form 40% of sales:** Top five brands including Ampilox (ampicillin + cloxacillin), Biotax (cefotaxime), Monotax (ceftriaxone + sulbactam), Amicin (amikacin) and Zithrocin (azithromycin) form c40% of group sales with all brands growing in double digits. Biochem's Biotax is the largest and Amicin is second-largest (after Aristo's Mikacin) in their categories. Monotax is also one of the fastest growing brands in the combination anti-infective space.

**Domestic formulations have been a drag in 1HFY12:** Domestic formulations top-line growth has slowed to 9% in 1QFY12 and c7% in 2QFY12 from 22.4% in Q4FY11 and now represents 38% of group sales. We believe that part of the reason for this slowdown is the reclassification of sales from domestic formulations to the Bayer JV, which we calculate has sales of cINR250mn quarterly. Following this acquisition we expect a marginal improvement in domestic growth for 2HFY12, given that higher sales will be partly offset by additional overheads (increase in sales force and other expenses). We expect India formulation to recover in FY13 from a low base and currently forecast c18% growth.

**US remains key driver, maintain OW:** The US (which now forms c25 % of group sales) should remain strong on the back of new approvals (including some limited competition opportunities such as gClarinx Reditabs where we believe Cadila is joint FTF with Dr Reddy's Labs). We do not include this acquisition in our estimates as we do not have details about Biochem's margin. We maintain our target price of INR930, based on 20x September 2013e EPS of INR46.5. Downside risks include slower ramp up in US and unanticipated declines from Hospira JV following Sandoz' entry in docetaxel.

## Financials & valuation

### Financial statements

Year to	03/2011a	03/2012e	03/2013e	03/2014e
<b>Profit &amp; loss summary (INRm)</b>				
Revenue	46,060	50,929	60,047	68,093
EBITDA	10,262	10,546	12,676	14,172
Depreciation & amortisation	-1,269	-1,400	-1,450	-1,500
Operating profit/EBIT	8,993	9,146	11,226	12,672
Net interest	-580	-495	-595	-415
PBT	8,425	8,666	10,646	12,272
HSBC PBT	8,425	8,666	10,646	12,272
Taxation	-1,064	-1,213	-1,597	-1,841
Net profit	7,110	7,203	8,799	10,231
HSBC net profit	6,844	7,126	8,799	10,231

### Cash flow summary (INRm)

Cash flow from operations	6,522	7,819	8,256	9,716
Capex	-4,579	-5,000	-5,000	-5,500
Cash flow from investment	-4,567	-5,250	-5,250	-5,700
Dividends	-1,529	-1,425	-1,760	-2,046
Change in net debt	-377	-1,067	-1,246	-1,970
FCF equity	1,931	2,804	3,241	4,201

### Balance sheet summary (INRm)

Intangible fixed assets	10,088	10,088	10,088	10,088
Tangible fixed assets	12,548	16,148	19,698	23,698
Current assets	23,036	26,511	31,254	36,336
Cash & others	3,159	3,595	4,210	5,548
Total assets	45,672	52,747	61,040	70,122
Operating liabilities	11,188	13,194	15,079	16,606
Gross debt	10,973	10,342	9,711	9,080
Net debt	7,814	6,748	5,502	3,532
Shareholders funds	21,715	27,415	34,454	42,639
Invested capital	31,325	35,959	41,752	47,967

### Ratio, growth and per share analysis

Year to	03/2011a	03/2012e	03/2013e	03/2014e
<b>Y-o-y % change</b>				
Revenue	25.2	10.6	17.9	13.4
EBITDA	26.9	2.8	20.2	11.8
Operating profit	33.3	1.7	22.7	12.9
PBT	39.5	2.9	22.8	15.3
HSBC EPS	34.7	4.1	23.5	16.3

### Ratios (%)

Revenue/IC (x)	1.6	1.5	1.5	1.5
ROIC	28.3	24.2	25.3	18.6
ROE	36.0	29.0	28.4	26.5
ROA	19.2	16.5	17.1	16.7
EBITDA margin	22.3	20.7	21.1	20.8
Operating profit margin	19.5	18.0	18.7	18.6
EBITDA/net interest (x)	17.7	21.3	21.3	34.1
Net debt/equity	34.9	24.0	15.7	8.2
Net debt/EBITDA (x)	0.8	0.6	0.4	0.2
CF from operations/net debt	83.5	115.9	150.1	275.1

### Per share data (INR)

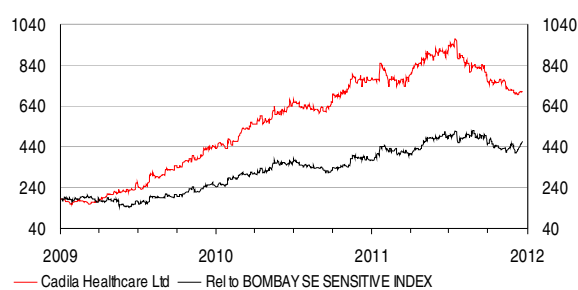
EPS reported (fully diluted)	34.73	35.18	42.97	49.97
HSBC EPS (fully diluted)	33.42	34.80	42.97	49.97
DPS	6.25	6.96	8.59	9.99
Book value	106.06	133.90	168.28	208.25

### Valuation data

Year to	03/2011a	03/2012e	03/2013e	03/2014e
EV/sales	3.3	3.0	2.5	2.2
EV/EBITDA	15.0	14.5	12.0	10.6
EV/IC	4.9	4.3	3.6	3.1
PE*	21.3	20.4	16.5	14.2
P/Book value	6.7	5.3	4.2	3.4
FCF yield (%)	1.3	1.9	2.2	2.9
Dividend yield (%)	0.9	1.0	1.2	1.4

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

### Price relative



Source: HSBC

Note: price at close of 20 Dec 2011

## Biochem portfolio snapshot

### Biochem: Antibiotics form c80% of total sales

Sales breakdown by therapy	MAT July' 11	MAT July' 10	MAT July '09
Anti-Infectives	81%	81%	80%
Cardiac	3%	3%	4%
Gastro Intestinal	3%	3%	3%
Others	13%	12%	13%

Source: IMS Health

### Biochem: Top 10 brands by sales (INRm)

Brand	MAT Jul'11	MAT Jul'10	MAT Jul'09	2-Yr CAGR
Biotax	470	410	340	17.5%
Amicin	405	380	318	12.8%
Ampilox	400	350	315	12.7%
Monotax	345	220	160	46.9%
Zithrocin	95	78	65	20.9%
Penclav	60	55	57	2.4%
Sulbacef	55	50	53	1.6%
Cefoxim	45	44	50	-4.9%
Biodoxi	36	30	27	15.1%
Biocillin	36	35	30	9.2%
Top 10 brands	1,947	1,652	1,416	17.3%
Top 10 brands as % of total	66.6%	65.6%	62.9%	

Source: IMS Health

### Biochem's Amicin features among Top 5 brands in its respective category in Indian formulation market

Brand	Corporate	MAT Jul'09	MAT Jul'10	MAT Jul'11	2 Yr CAGR
Mikacin	Aristo Pharma	831	974	1,014	10.5%
Amicin	Biochem	317	383	405	13.1%
Mikastar	Mankind	190	239	238	11.8%
Amitax	Alkem	186	171	173	-3.4%
Ivimicin	FDC	126	176	166	15.0%
Total Amikacin		2,074	2,621	2,885	18.0%

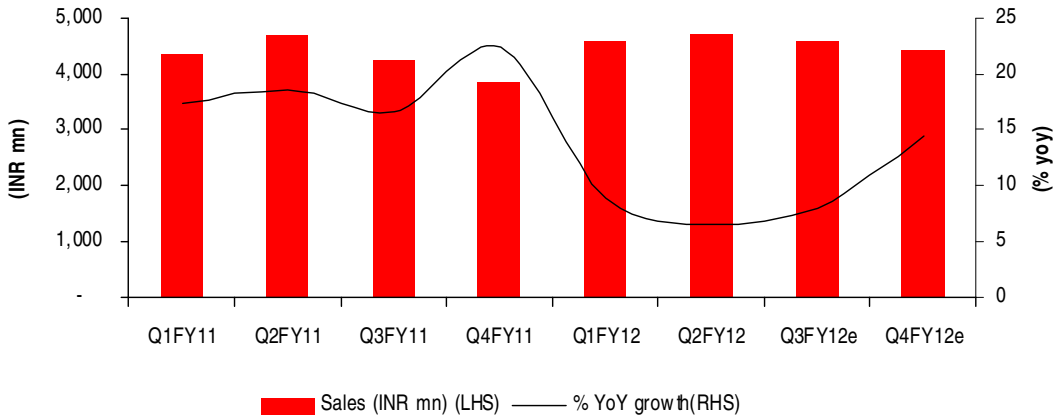
Source: IMS Health

### Biochem's Monotax features among Top 10 brands in its respective category in Indian formulation market

Brand	Corporate	MAT Jul'09	MAT Jul'10	MAT Jul'11	2 Yr CAGR
Monocef	Aristo Pharma	1,273	1,586	1,884	21.6%
Xone	Alkem	437	523	573	14.5%
Oframax	Ranbaxy	339	386	464	16.9%
Traxol	Alkem	223	274	287	13.4%
Finecef Inj	Abbott	4	125	268	694.3%
Monotax	Biochem	140	176	241	31.3%
Accuzon	Macleods Pharma	83	139	211	59.1%
Cefaxone	Lupin Limited	197	186	190	-1.9%
Powercef	Wockhardt-Merind	40	83	151	94.4%
Extacef-I	Blue Cross	126	145	150	9.3%
Total Ceftriaxone injectables		4,106	4,861	5,771	18.5%

Source: IMS Health

Cadila: domestic formulation quarterly growth trends



Source: Company data, HSBC

## Valuation and risks

We continue to value Cadila at 20x (in line with its five-year historical average) September 2013e EPS of INR46.5 to arrive at our 12-month TP of INR930. We reiterate our OW rating on the stock as fundamentals are intact and our TP implies 31.9% potential return. Our investment thesis is unchanged and we continue to like Cadila's small but strong niche business, one of the top domestic businesses and R&D focus to deliver long-term growth drivers like biosimilars, vaccines and NCEs. The downside risk to our view includes slower ramp up in US and unanticipated declines from Hospira JV following Sandoz' entry in docetaxel.

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 target price implies a potential return of 31.9%, which is above the Neutral band of our model; therefore, we rate the stock Overweight. Potential return equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated.

# Disclosure appendix

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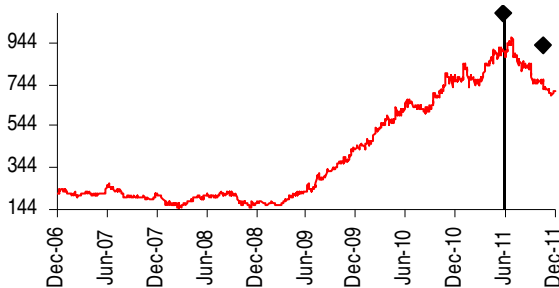
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<b>Overweight (Buy)</b>	54%	(25% of these provided with Investment Banking Services)
<b>Neutral (Hold)</b>	35%	(19% of these provided with Investment Banking Services)
<b>Underweight (Sell)</b>	11%	(13% of these provided with Investment Banking Services)

## Share price and rating changes for long-term investment opportunities

Cadila Healthcare Ltd (CADI.BO) Share Price performance INR Vs HSBC rating history



Source: HSBC

### Recommendation & price target history

From	To	Date
N/A	Overweight	16 June 2011
Target Price	Value	Date
Price 1	1085.00	16 June 2011
Price 2	930.00	10 November 2011

Source: HSBC

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