

Indian Pharma Sector

Global Generics: Patent cliff around?

Table Of Contents

Sr. No.	Content	Page
1	Executive Summary	3
2	Generic market to remain buoyant	4
3	So Far So Good	7
4	Its Not A Smooth Ride All Way	15
5	Valuation Matrix	18
6	Company Snapshots	19-59
	Aurobindo Pharma	19
	Biocon	23
	Cadila Healthcare	27
	Cipla	31
	Divi's Laboratories	35
	Dr Reddy's Laboratories	39
	GlaxoSmithkline Pharma	43
	Glenmark Pharmaceuticals	45
	Ipca Laboratories	49
	Lupin	53
	Sun Pharmaceuticals	57

Global Generics: Patent cliff around?

The Indian pharma players have been one of the biggest beneficiaries of the patent cliff over the last five years. Over time, some of these players have built up sizeable base in the US markets through their systemic approach to tap into the opportunities going off patent, while some have opted to take the direct route through acquisitions. How long can this go on? And how prepared are the Indian players and which ones, to tackle this opportunity as it tapers off next few years? And can there be there other geographies that can present as growth avenues for the companies? We attempt to take a macro view on these issues in this note.

GLOBAL GENERICS

The global generics market is estimated to grow to USD 430bn in 2016 from USD 242bn in 2011, implying a CAGR of 12%. This compared to the 8% CAGR over 2006-2011 is a marked acceleration. The near-term outlook for US generics remains intact with USD 100bn worth of drugs slated to go off patent over the next five years.

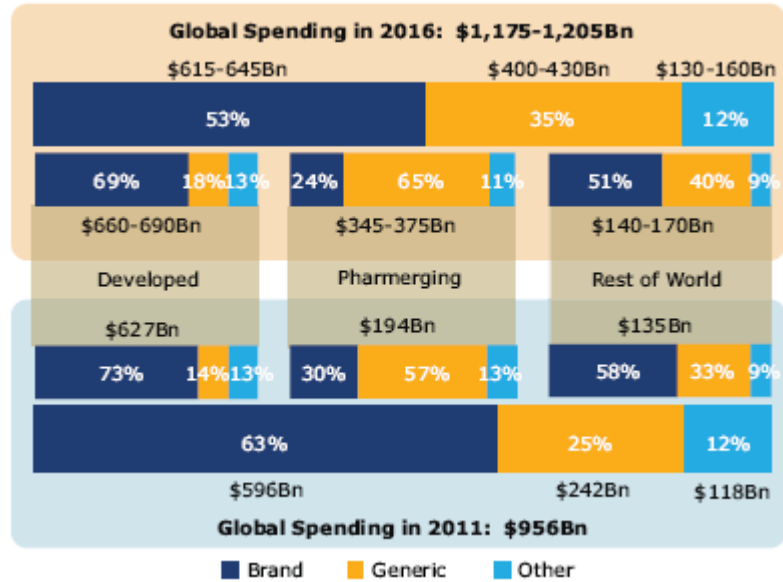
While the upcoming patent cliff may throw up selective opportunities for Indian generic companies, we do believe that low lying fruits that created opportunity to reap significant rewards are done. Hence it would require a more selective approach on part of the Indian drug makers to scale up on capabilities towards complex molecules, as well as focus on new areas. We believe Indian generic companies are gearing up for this opportunity through a) Shifting focus towards differentiated platform technologies, b) Niche/complex filings, focusing more on profitability than market share, c) Aggressive Para IV filings, d) Building branded portfolio to tap specialty therapies, e) Orphan/Shortage drugs: future potential for Indian generics, f) M&A activity: tap the complex/ niche opportunity and g) Tie-up/In-licensing deals with innovators.

However, challenges such as a) Growing ANDA approval backlog and increasing ANDA approval timelines, b) USFDA's increased focus on cGMP compliance, c) unfair use of restricted drug distribution program by innovators have impacted sentiment.

Generic market to remain buoyant

The global generic market is expected to increase from US\$242bn in 2011 to US\$430bn by 2016. This growth would be largely driven by patent expiries in developed markets, expanded generic use for off-patent molecules and volume-driven growth in the pharmerging markets.

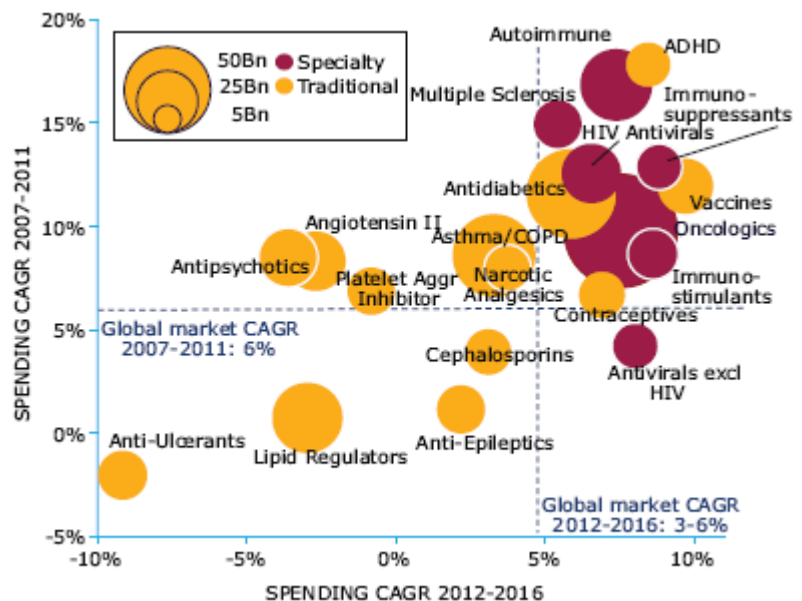
Global Spending, 2011 and 2016



Source: IMS Institute for Healthcare Informatics, IMS Market Prognosis, May 2012

Specialty therapies to drive growth: Specialty medicines will experience continued growth driven by novel mechanisms, improved efficacy and relatively large patient populations leading to increased uptake. However, growth is decelerating in most therapy areas due to patent expiries and the lack of significant new treatment options. Of the 20 largest therapy areas, only classes with anti-epileptics, contraceptives and antivirals (excl.HIV products) will grow faster than in the past 5 years.

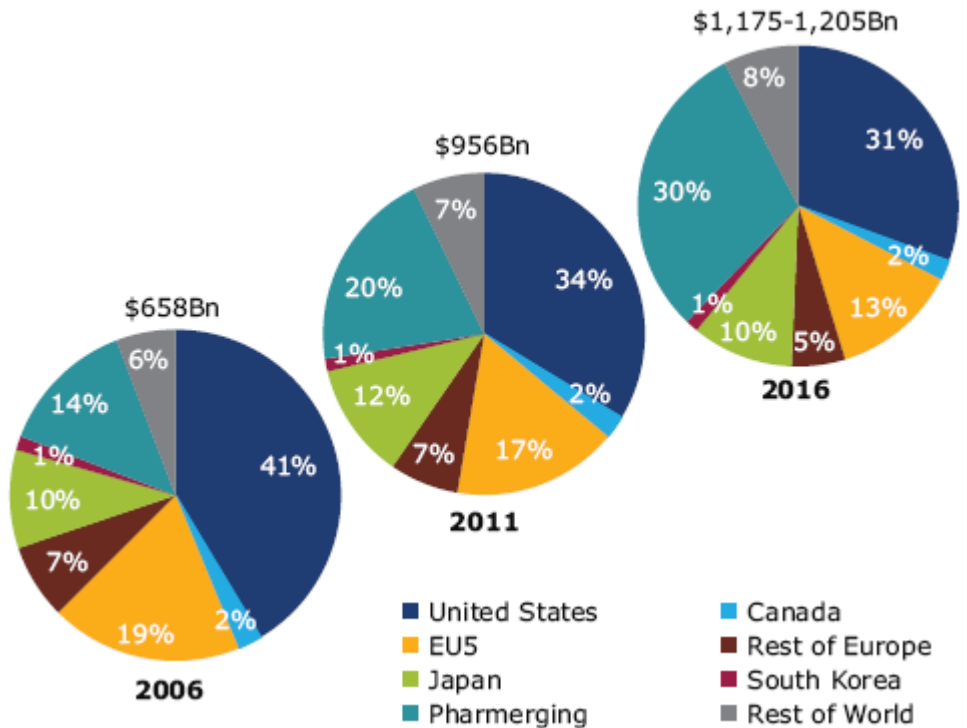
Spending and Growth in Leading Therapy Areas



Source: IMS Institute for Healthcare Informatics, May 2012

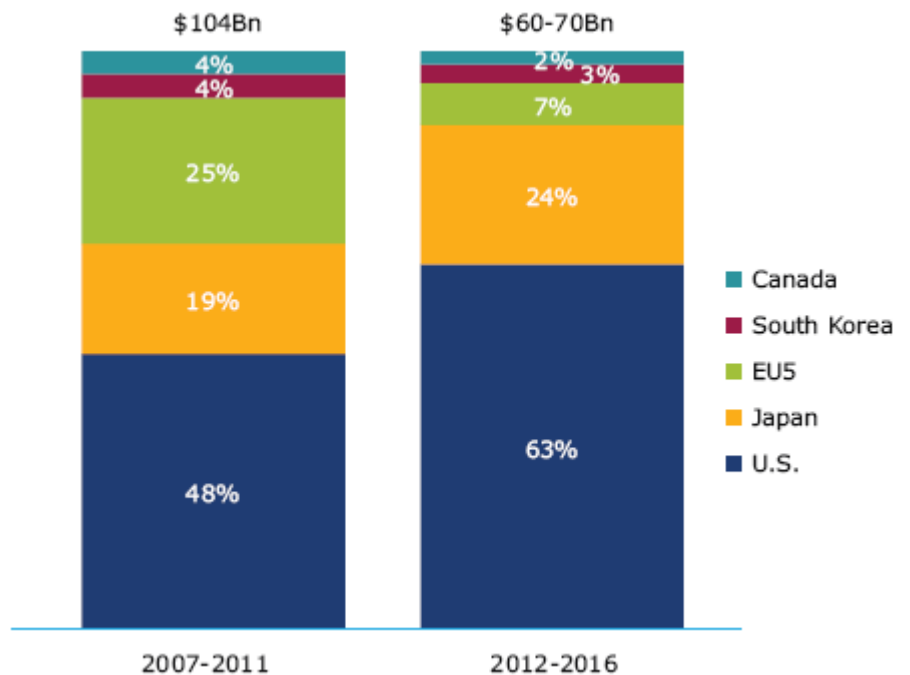
US share to decline, however continues to be the largest in absolute terms: The US share of global spending on generics is expected to decline from 34% in 2011 to 31% in 2016, while the share of top five European countries is expected to decline from 17% to 13%. The biggest gainer shall be the pharmerging markets going up from USD 194bn in 2011 to USD 359bn in 2016. However in absolute terms, US market will continue to be the biggest market expanding in generic spending from US\$325bn in 2011 to US\$364bn in 2016.

Spending by Geography



Source: IMS Market Prognosis, May 2012

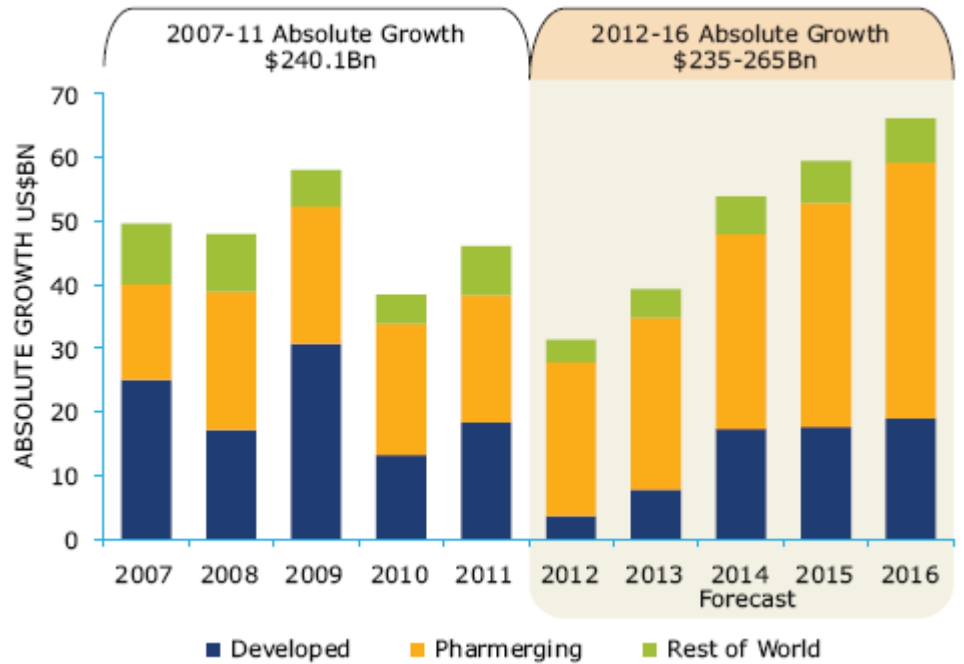
Contribution to Developed Market Growth



Source: IMS Market Prognosis, May 2012

Pharmerging markets to grow at 13% CAGR over next five years:
 The Pharmerging markets are expected to nearly double their pharmaceutical spending from US\$194bn in 2011 to US\$359bn in 2016 and would reach 30% of global spending in 2016, as rising incomes, combined with continued low costs for medicines, will drive significant increase in affordability of basic medicines.

Global Growth 2007-2016



Source: IMS Market Prognosis, May 2012

So Far So Good

Indian companies moving up the value chain in US

Indian companies have tapped the US market by focusing on opportunities in plain-vanilla generics segment. However, many Indian companies continued to improve their product offerings and look at alternative avenues to generate higher revenues/margins and accelerated growth. These included:

- 1) Difficult-to-make products having technological barriers to entry either in terms of API manufacture or dosage formulations
- 2) Niche category products that require dedicated facilities/clinical trials and are not economically viable for more than few generic players. e.g., Cephalosporins, dermatology, controlled substances, hormonal products etc.
- 3) Paragraph IV opportunities (several generic companies are also settling litigation with innovators, thereby ensuring upside and removing litigation risks) and
- 4) Focus on specialty branded products, e.g. Suprax, Antara (Lupin); Promius pharma – Branded specialty company of Dr Reddy's, DUSA acquisition by Sun pharma for entry into branded dermatology segment.

While the upcoming patent cliff may throw up selective opportunities for Indian generic companies, we do believe that low lying fruits that created opportunity to reap significant rewards are done. Hence it would require a more selective approach on part of the Indian drug makers to scale up on capabilities towards complex molecules, as well as focus on new areas. We believe Indian generic companies are gearing up for this opportunity through.

- A) Differentiated platform technologies
- B) Niche/complex filings for the US market
- C) Aggressive Para IV filings
- D) Building branded portfolio to tap specialty therapies
- E) Orphan Drugs: Future potential for Indian generics
- F) Adding differentiated products/technology through acquisitions
- G) Tie-up/In-licensing deals

Firms such as Sun pharma, Dr Reddy's and Lupin have created operating niches to derive sustainable growth. For example, Sun continues to operate primarily in the niche, high margin areas of CNS and CVS, and has now forayed into highly profitable dermatology segment through the acquisition of Dusa.

DRL has entered into an alliance with Merck to co-develop a portfolio of biosimilar compounds in oncology, primarily focused on monoclonal antibodies (MAbs). This alliance offers a risk mitigation pathway for DRL to take its development capabilities through the clinical phase and then into commercialization.

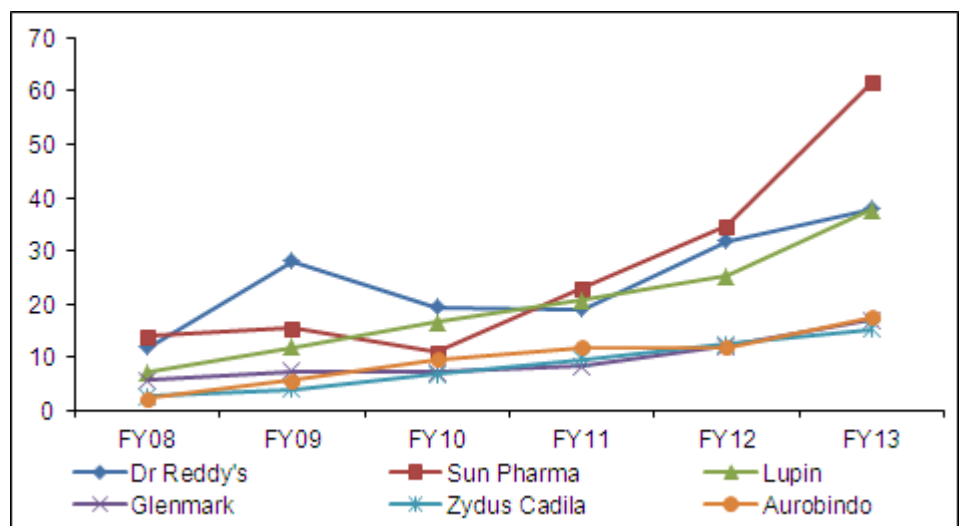
Similarly, Lupin has identified ophthalmology, dermatology and respiratory as its medium-term growth drivers. In addition to filing products on its own, the company is also exploring inorganic opportunities in this space to fill contraceptive segment, with eight products pending approval from USFDA.

Key products/segments tapped

Company	Key Products launched	Focus areas
Dr Reddys	gGeodon, gZyprexa, gPropecia, gArixtra, gAccolate, glimitrex, gPrilosec, gPrevacid, gPrograf, gAllegra D24, gReclast, gZenatane, gDacogen	Para IV products, injectables, CNS
Sun Pharma	gTrileptal, gProtonix, gEthyol, gEloxatin, gExelon, gGemzar, gTaxotere, gLexapro, gGabitril, gStalevo, glimitrex inj	Controlled substances, dermatology,
Lupin	Suprax, Antara, Ocs, gGeodon, gDiovon, gTricor, gSeasonale, gCombivir, gSeroquel, gGlumetza, gCymbalta, AG Femcon Fe, gKeppra XR, gLotrel	OC's, Branded products, dermatology
Glenmark	gOvcon-35, gOrtho-Novum 1/35, 7/7/7, gDifferin, gCutivate, gLoprox, gAldara, gMircette, gLamictal, gSingulair, gMaxalt, gBactroban	Dermatology, Controlled substance, OC's

Source: Dolat Research

US Sales of Indian Companies



Source: Dolat Research

A. Shifting focus towards differentiated platform technologies

Indian generic companies are moving from plain-simple oral generics to differentiated generics based on novel delivery systems including injectables, sprays, aerosols, topical. This strategy not only helps in keeping competition away for a longer period of time, but also provides better pricing environment.

Sun Pharma has moved from simple dosage forms like tablets and capsules to differentiated/complex products. The company has developed different drug delivery platform technologies like novel device for inhaled drugs (dry powder inhalation device for uniform dose administration), gastro retentive device for controlled release products (allows longer retention of drugs in stomach and improves GI absorption), targeted drug delivery for nanoemulsions (selective delivery of cytotoxic drugs), bio-degradable injections/implants.

B. Niche/complex filings

As patent cliff looms, Indian generic companies are building a differentiated product pipeline not only in anti-infectives, CVS and CNS therapies but also niche therapies such as oral contraceptives, dermatology, ophthalmic and controlled substances. Additionally, most Indian companies are focusing on quality filings over quantity to mitigate the risk of volatility on account of sharp price erosions in plain vanilla generic drug market.

Focus on niche/complex therapies

Niche/complex therapies	Sun Pharma	Dr. Reddys	Lupin	Ranbaxy	Glenmark	Zydus Cadila	Cipla
Dermatology							
Controlled Substances							
Ophthalmology							
Injectables							
Inhalers							
Oral Contraceptives							
Biologics							
Oncology							
Transdermal							

Source: Dolat Research

C. Aggressive Para IV filings

Over the next five years, drugs worth USD 100 bn shall go off-patent. Based on our estimate, we believe that Indian generic companies are targeting USD 40-45bn of opportunity through Para IV filings. Among the Indian generic companies, Dr Reddy's, and Lupin have been the most prolific filers for Para IVs due over the next five years, followed by Sun Pharma, Glenmark and Aurobindo respectively.

Top 5 brands going off-patent in next five years

Brands	Innovators	Indication	Sales (USD mn)	Year	Filer	Remarks
Cymbalta	Lilly	Depression	3400	2013	Aurobindo, DRL, Impax, Lupin, Sandoz, Sun, Teva, Torrent, Wockhardt, Zydus	Marketing excl. ends in Dec-13. As there has been no settlement, we believe nobody will have exclusivity. 9 players have received tentative approval.
Nexium	Astra Zeneca	GERD	3944	2014	Ranbaxy, Lupin, Dr. Reddy's, Sandoz, Hetero, Torrent, Mylan, Teva	Ranbaxy has an FTF and settled for launch on May 27, 2014. Other filers such as DRL and Teva have settled for launch in November 2014. Sandoz/Lupin have settled. Terms have not been disclosed.
Clarinet	Sepracor	Asthma/Allergic I	3000	2014	Multiple companies	There are 13 generic companies that have filed a Para IV. We believe the upside for most of the companies will not be material, in case of a positive outcome.
Celebrex	Pfizer	Pain	1580	2014	Actavis, Mylan, Teva, Apotex, Lupin	Pfizer filed a patent infringement lawsuit against Lupin, Mylan, Apotex, Teva, Watson on March 05, 2013. Generic competition is expected post patent expiry on Dec 2nd, 2015.
Abilify	Otsuka	Schizophrenia, bipolar disorder	4790	2015	Alembic, Barr, Sun, Torrent (tablet); Zydus (orally disintegrating tablet)	Teva/Barr is anticipated to launch generic ABILIFY oral solution with 180-day exclusivity after the pediatric exclusivity associated with the '528 patent expires on April 4, 2015.

Source: Dolat Research

D. Building branded portfolio to tap specialty therapies

As the US generic market is moving away from plain vanilla generics to specialty/complex products, it is becoming imperative for Indian generics to build branded portfolio. Most Indian large-cap generics have small presence in branded products within the US with marginal contribution to bottom line except for Lupin. This is in contrast to Teva where the branded portfolio accounts for well over half of the company's profitability.

However, branded business remains a risky proposition given the risk of generic entry and expensive acquisition multiples. Nonetheless, Indian pharma is seen investing more in building business in this segment given stability in revenues and pricing advantage.

Branded portfolio of Indian companies in US

Company	Branded Product
Lupin	Suprax, Antara, Allernaze (pipeline)
Dr Reddy's	Promiseb, Cloderm, Scytera, Epiceram (Specialty dermatology business under Promiuspharma)
Sun Pharma	Ovide, Topicort, Lustra (Taro), Levulan PDT (DUSA)
Cipla	Dymista (Partnership with Meda)
Ranbaxy	Absorica (Isotretinoin), Ximino (Minocycline HCL)

Source: Dolat Research

E. Orphan Drugs: Future potential for Indian generics

Orphan drug designation is given by the FDA to drugs, which are intended to treat rare diseases that affect less than 200,000 patients in the US. The FDA extends special incentives for companies developing orphan drugs such as seven-year marketing exclusivity, specific tax credits on R&D expenses and waiver of prescription drug user fees. Also, these drugs are approved through a fast track approval process by the FDA, which is to facilitate early commercial launch of the drug.

The orphan drugs market grew at a CAGR of 25.8% from 2001 to 2010 versus a CAGR of 20.1% for non-orphan drugs. In another recent study by Evaluate Pharma, orphan drug market is set to grow to USD127bn, at a CAGR of 7.4% between 2012 and 2018, and increase its share in overall prescription market(excluding generics) to 15.9% by 2018 from 5.1% in 1998.

Natco pharma's novel anti-cancer drug NRC-AN-019 has received 'Orphan Drug Designation' from the USFDA for three indications namely Glioma (brain tumor), pancreatic cancer and chronic myelogenous leukemia.

We expect these products present interesting opportunities for Indian generic companies like Dr Reddy's, Sun Pharma, Strides Arcolab, Zydus Cadila and Biocon.

Orphan drugs approved in 2012

Product	Company	Molecule	Indication
Elelyso	Pfizer	Taliglucerasealfa	Gaucher's disease
Kyprolis	Onyx Pharma	Carfilzomib	Multiple Myeloma
Bosulif	Pfizer	Bosutinib	Chronic myelogenous leukaemia
Kalydeco	Vertex Pharma	Ivacaftor	Cystic fibrosis
Jakafi	Incyte Corp	Ruxolitinib	Bone Marrow disease
Erwinaze	EUSA Pharma	Asparaginase Erwinia Chrycanthemic	Acute lymphoblastic leukemia
Onfi	Lundbeck	Clobazam	Seizures associated with Lennox-Gastaut syndrome
Voraxaze	Btg international, inc	Glucarpidase	Toxic methotrexate concentrations in plasma of patients receiving chemotherapy
Ferriprox	ApopharmaInc	Deferiprone	Iron overload

Source: FDA

F. Adding differentiated products/technology through acquisition route:

In 2012, Indian companies completed four global acquisitions (~USD1 bn) to add differentiated products to their portfolio.

Sun Pharma acquired DUSA pharma for ~USD 230mn to gain entry into the drug-device dermatology market. DUSA's key flagship product is Levulan PDT (photodynamic therapy) for treatment of non-hyperkeratotic actinic keratoses or AKs of the face or scalp.

Dr Reddy's acquired OctoPlus NV for ~USD 36mn to get entry in long-acting controlled release technology, which can be applied to various products. DrReddys would capitalize on OctoPlus's expertise in injectable specialty generics such as liposomes and microspheres. OctoPlus's key asset is Locteron, which is a controlled release interferon alpha2b based on proprietary PolyActive technology.

We expect the acquisition route to be one of the most critical in the pursuit of Indian companies to graduate on capabilities.

Indian pharma on the roll

Company	Target	Acquisition value	% stake	Rationale
Sun Pharma	URL Pharma	Details not disclosed	100%	Non-Colcrys generic assets
	DUSA Pharma	USD 230mn	100%	Adds Levulan PDT asset
	Taro	USD 454mn	66%	Dermatology & topical product portfolio
	Caraco	NA	100%	Dosage form plant
Cipla	Cipla Medpro	USD 512mn	100%	Provides front end operations in Africa
Dr Reddys	OctoPlus NV	~USD 36mn	98.6%*	Provides drug delivery technology
	Betapharm	USD 560mn	100.0%	Entry in German market
	BMS labs	USD 12mn	100.0%	Entry in UK's generic market
	Roche's API facility, Mexico	USD 59mn	NA	Adds steroids manufacturing capabilities
Lupin	I'rom	NA	100.0%	Entry in injectable market in Japan
	Kyowa	Details not disclosed	100.0%	Entry in Japan market
	Pharma Dynamics, South Africa	Details not disclosed	60.0%	Entry in SA market
	Generic Health, Australia	Details not disclosed	91.0%	Entry in Australian market
	Hormosan Pharma, Germany	Details not disclosed	100.0%	Entry in German CNS market
	Multicare Pharma, Philippines	Details not disclosed	51.0%	Entry in branded generics segment in women's health and child care segment in Philippines

Source: Dolat Research

G. Tie-up/In-licensing deals:

An interesting fall-out of Big Pharma's new operating paradigm involving aggressive branded generics play in EMs, along with generics in regulated markets, has been the hitherto unthinkable partnering of Global Pharma players and Indian generics. These partnerships have been catalyzed by Big Pharma's need for low-cost, reliable and world class manufacturers with the ability to develop and register a large suite of products across multiple geographies. This is critical for them to operationalize their EM/generic strategies without having to go through the lengthy process of developing these multiple products and then sinking in significant capex for manufacturing capabilities. Indian generics companies benefit by getting the formidable marketing resources of MNC pharma to sell their products – and thereby improve the likelihood of garnering higher market share across products as well as enhance capacity utilization. Some of the key deals in this segment include:

Tie-up/In-licensing deals

Innovator	Generic company	Target markets	Products
Pfizer	Claris	US, Canada, New Zealand	15 sterile injectables
	Strides Arcolabs	US, Canada, New Zealand, Australia, Japan and Korea	45 products (mainly oncology injectables)
	Aurobindo Pharma	US, Canada, Rest of Europe, ROW, Australia, NZ	~100 products (includes orals and injectables)
Astra Zeneca	Torrent Pharma	ROW	18 products for 9EMs
	Aurobindo Pharma	Emerging Markets	Formulation and sterile products
GSK Pharma	Strides and Onco Therapeutics	EM outside India and Africa	Injectables
	Dr Reddy's	Africa, LATAM, Asia Pacific	Co-marketing and revenue sharing
Abbott Labs	Acquired domestic formulation biz of Piramal Healthcare	India	To be no.1 in India, post this acquisition
	Cadila HC	15 markets	Initially for 24 products, to be extended to 40 products later
MSD	Sun Pharma	Emerging Markets	Innovative branded generics (largely combination products)
Mylan	Famy Care		Develop and supply 22 OC's
Bayer	Cadila HC		50:50 JV
Eli Lilly	Lupin	India and Nepal	Promote Huminsulin (Lilly's products)
Merck	Serum Institute	Emerging Markets	Develop and commercialise a pneumococcal conjugate vaccine (PCV)
DSM Pharma	Indoco Remedies	Austria and other international markets	Eight APIs
Sanofi Pasteur	Emcure	India	Sanofi's anti-rabies vaccine - Verorab; to be imported/supplied by Sanofi and marketed/distributed by Emcure
Roche	Emcure	India	Emcure will manufacture anti-cancer biologics drugs; Herceptin and MabThera. The agreement has potential to expand to other countries

Source: Dolat Research

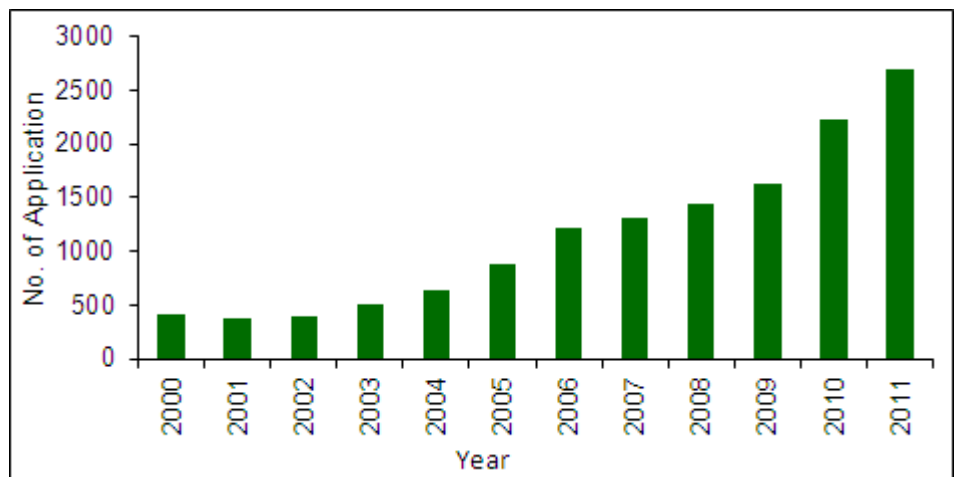
ITS NOT A SMOOTH RIDE ALL WAY!

A. Growing ANDA approval backlog and increasing ANDA approval timeline: The Office of Generic Drugs of US is facing an acute shortage of resources to review generic drugs. This has resulted in increased ANDA approval timelines, consequently leading to growing ANDA approval backlog.

To address this issue, the Office of Compliance and OGD has established a prioritization scheme for inspections that are required to support ANDA's and ANDA supplements. A general description of this prioritization scheme follows:

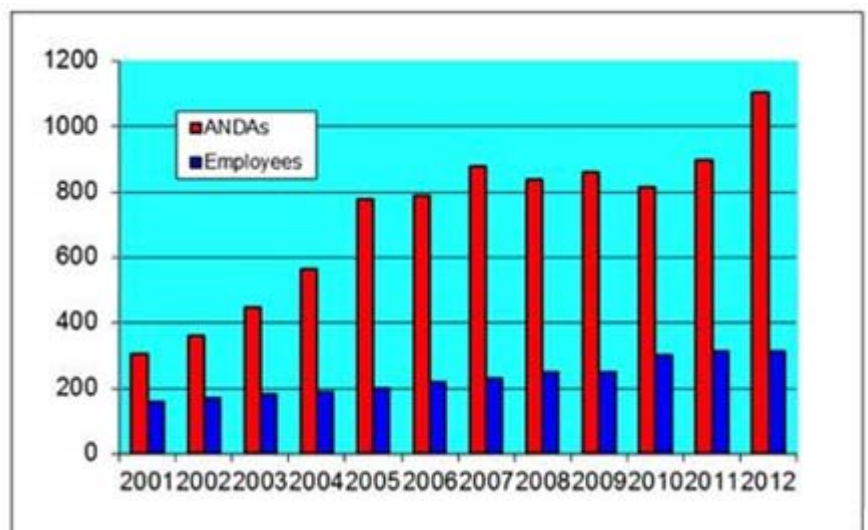
- Drug shortage situations are given the highest priority for inspection.
- The next priority tier involves ANDAs that contain a Para IV certification for which a potential 180-day exclusivity entitlement exists.
- The last priority tier involves applications for products that have been impacted by unforeseen circumstances that have caused a firm to stop production (i.e., acts of nature that have caused damage or obliteration of a facility).

Office of generic drugs backlog.



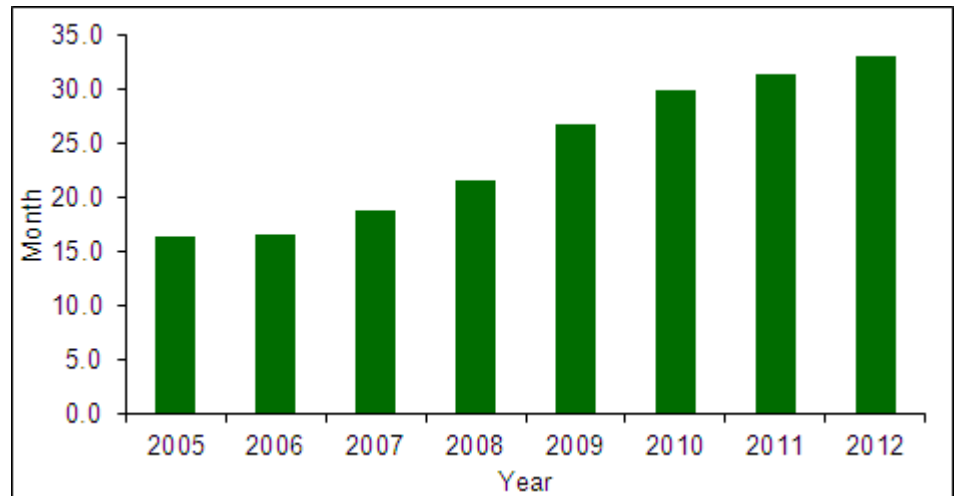
Source: FDA

Generic applications vs employees.



Source: FDA

Increasing ANDA approval timeline

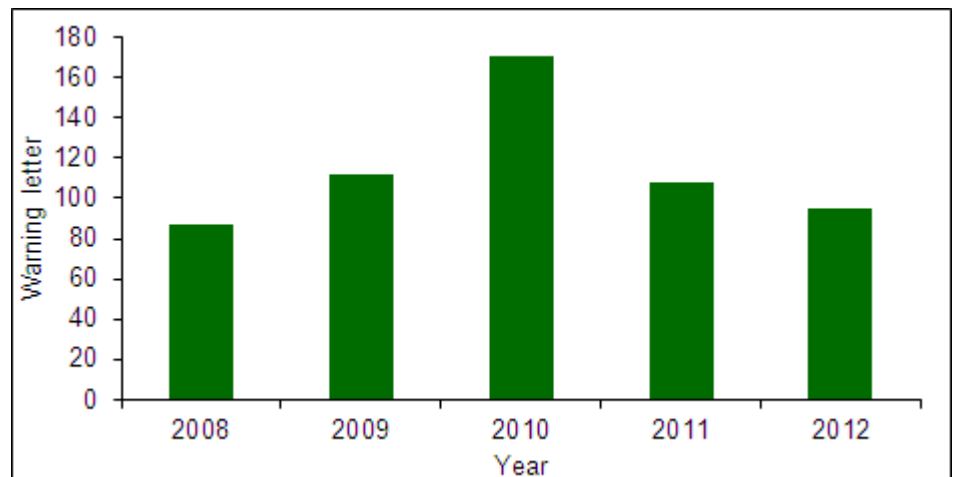


Source: FDA

B. USFDA's increased focus on cGMP compliance: In 2013, the DOJ (Department of Justice) has announced that it would be taking a hard look at violations under current good manufacturing practices (cGMPs). The DOJ plans to actively step up enforcement for cGMP violations under the authority of False Claims Act (FCA), in addition to Federal Food, Drug, and Cosmetic Act (FFDCA).

The USFDA found violations at 558 drug plants inspected in 2010, or 54% of all plants inspected in 2010, an increase of 20% from 2007. In addition, FDA center for Drug Evaluation and Research issued 95 drug related warning letters in 2012, down from a peak of 171 warning letters in 2010.

FDA warning letter from 2008-2012



Source: FDA

Warning letters to Indian companies

Companies	Facility	Location	Year	Remarks
Aurobindo	Unit III & VI	Hyderabad	2011	Cleared
Claris Lifesciences	Clarion II	Ahmedabad	2010	Cleared
Dabur	Bordon	UK	2009	Pending
Dr Reddy's	Cuemavaca	Mexico	2011	Cleared
Fresenius	Nadia	West Bengal	2013	Pending
Lupin	Bhopal	Madhya pradesh	2009	Cleared
Ranbaxy	Paonta Sahib	Himachal Pradesh	2008	Pending
	Dewas	Himachal Pradesh	2008	Pending
	Ohm Labs	New York	2009	Pending
RPG Lifesciences	Ankleshwar	Gujarat	2013	Pending
	Navi Mumbai	Maharashtra	2013	Pending
Sun pharma/ Caraco	Detroit	Michigan	2008	Partially cleared*
	Cranbury	New Jersey	2010	Cleared
Wockhardt	Waluj	Maharashtra	2013	Pending
Zydus Cadila	Moraiya	Gujarat	2011	Cleared

Source: Dolat Research

C. Unfair use of restricted drug distribution program by innovators:

Certain brand drugs are subject to distribution restrictions that may be used to prevent generic firms from accessing samples (for bioequivalence testing) of brand product. This is being implemented as part of FDA mandated risk management programs known as REMS (Risk Evaluation and Mitigation Strategies). However, the FTC (Federal Trade Commission) has found that branded name drug manufacturers are improperly using restricted drug distribution programs to impede generic competition.

Nearly 40% of new drugs are currently subject to FDA-imposed safety restrictions, and innovators are taking advantage to block competition.

Valuation Matrix

Companies	Net Sales (₹ mn)			EBIDTA (₹ mn)			PAT (₹ mn)			EPS (₹)		
	FY13	FY14E	FY15E	FY13	FY14E	FY15E	FY13	FY14E	FY15E	FY13	FY14E	FY15E
Aurobindo	57,701	68,967	80,853	8,609	12,261	14,583	1,304	4,378	7,514	10.1	19.7	25.8
Biocon	24,853	29,286	33,797	5,430	6,516	7,672	5,088	3,885	4,693	15.3	19.4	23.5
Cadila Healthcare	63,581	69,709	81,864	11,257	12,199	14,736	6,553	7,302	9,299	32.0	35.7	45.4
Cipla	82,025	94,000	106,709	21,193	24,144	27,609	15,073	16,797	19,212	18.8	20.9	23.9
Divi's Labs	21,448	25,370	29,907	7,132	9,894	11,649	5,000	7,453	8,912	37.7	56.1	67.1
Dr. Reddy's Labs	118,745	129,701	146,568	27,347	29,292	33,172	16,090	17,304	20,227	102.8	101.9	119.1
Glenmark	50,123	58,548	68,840	10,113	12,046	14,479	6,147	7,201	8,944	22.7	26.6	33.0
GSK Pharma*	26,303	28,182	31,593	8,191	7,489	8,711	6,772	6,385	7,311	79.9	75.4	86.3
IPCA Labs	28,131	32,711	38,322	6,232	7,274	8,681	3,867	4,582	5,515	30.6	36.3	43.7
Lupin	96,413	111,299	128,689	22,700	26,155	30,885	13,404	15,572	17,990	30.0	34.8	40.2
Sun Pharma	112,389	132,833	160,487	49,673	58,295	68,512	35,916	44,696	49,978	34.7	21.6	24.1

* December year ending

Companies	Mcap (₹ bn)	CMP (₹)	TP (₹)	Upside (%)	P/E (x)			ROE(%)			EV/EBITDA(x)			Mcap/Sales (x)		
					FY13	FY14E	FY15E	FY13	FY14E	FY15E	FY13	FY14E	FY15E	FY13	FY14E	FY15E
Aurobindo	53	183	258	41	18.1	9.3	7.1	5.3	15.3	21.8	9.9	6.7	5.6	0.9	0.8	0.7
Biocon	68	339	399	18	22.1	17.5	14.5	12.4	13.8	15.1	11.7	10.0	8.6	2.7	2.3	2.0
Cadila Healthcare	131	642	727	13	20.0	18.0	14.1	23.5	22.5	24.4	13.3	12.1	10.0	2.1	1.9	1.6
Cipla	326	406	480	18	21.6	19.4	17.0	18.1	17.3	17.1	15.8	13.4	11.5	4.1	3.5	3.1
Divi's Labs	127	956	1,141	19	25.4	17.0	14.2	22.1	28.1	27.8	17.9	12.8	10.9	5.9	5.0	4.3
Dr. Reddy's Labs	375	2,210	2,382	8	21.5	21.7	18.6	24.9	21.6	20.7	14.3	13.0	11.0	3.2	2.9	2.5
Glenmark	139	514	561	9	22.7	19.3	15.6	29.7	33.1	31.3	15.4	12.6	10.1	2.8	2.4	2.0
GSK Pharma*	193	2,282	1,900	(17)	28.5	30.3	26.4	34.5	31.0	33.5	21.1	23.1	19.7	7.4	6.9	6.2
IPCA Labs	82	647	743	15	21.1	17.8	14.8	27.3	26.0	25.3	14.2	12.1	10.1	3.0	2.5	2.2
Lupin	376	840	965	15	28.1	24.2	20.9	29.3	26.8	24.9	16.8	14.0	11.7	4.0	3.4	3.0
Sun Pharma	1,057	510	603	18	14.7	23.7	21.2	29.7	33.1	31.3	9.9	17.4	14.1	4.7	8.0	6.6

* December year ending

CMP: ₹ 183

Target Price: ₹ 258

Buy

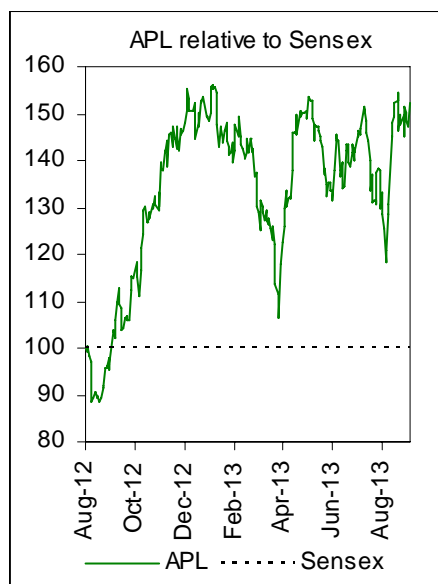
BSE Sensex	18,235
NSE Nifty	5341

Scrip Details

Equity	₹ 291mn
Face Value	₹ 1/-
Market Cap	₹ 53bn
	USD 794mn
52 week High / Low	₹ 205 / 102
Avg. Volume (no)	2785621
BSE Code	524804
NSE Symbol	AUROPHARMA
Bloomberg Code	ARBP IN
Reuters Code	ARBN.BO

Shareholding Pattern as on June'13(%)

Promoter	54.84
FII's	17.87
MF/Banks/FIs	13.78
Public / Others	13.51



Multi-Year Play on Injectables...

Aurobindo Pharma (APL), in the last five years, has transformed itself from being a low-margin API player to a high-margin formulation manufacturer. APL has identified injectables as a key focus area. It is investing upfront to build a strong pipeline of 100 ANDAs from current 30 ANDAs. Further, it has acquired assets (Celon plant) to accelerate growth in hormones/oncology and expects to file for 22 products from acquired site. These assets would render higher growth and margins. With an emerging new business model, we expect APL to have a robust performance on the back of strong US sales, new ARV tenders and growing traction in EU formulations.

Investment Rationale

Business Model - Realigned towards high margin formulations

APL has re-aligned its business model successfully over the last five years with an increasing focus on lucrative formulations business from low margin API earlier. Contribution of formulations to business mix has increased from 39% in FY08 to 57% in FY13, and we expect this to reach to 64% by FY15E. US, EU (50% of formulation sales) would be the key growth drivers in formulations as Aurobindo leverages its strong regulatory pipeline and ramps up supplies to licensing partners globally. Aurobindo's regulatory pipeline boasts of 281 ANDAs, 167 DMFs (drug master files), 1825 MAAs (marketing authorisation application—EU, RoW filings) which is supported by strong backward integration, ensuring price competitiveness in growing generic markets.

US Biz – Focus on niche segments

US generics segment contributed 30% of total sales in FY13. The company is focusing on high value niche segments such as injectables, controlled substances, penems, and hormones for future growth. The company has filed 281 ANDAs with the USFDA, of which 90 ANDAs are pending approval. We estimate US sales to register 26% CAGR over FY13-FY15E.

- **Injectable Segment** - APL has decided to spin off the injectable business to a wholly owned subsidiary to strengthen and increase its focus on high margin business. Currently, APL has filed 50 ANDAs (30 ANDAs from Unit IV and 20 ANDAs from Unit XII) with the USFDA and received approval for 25 ANDAs. The company has launched

Financials

Year	Net Sales	% Growth	EBIDTA	OPM %	Adj.PAT	% Growth	Adj.EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12	45,647	10.6	5,860	12.8	1,976	(63.8)	6.8	(63.8)	26.9	8.3	7.8
FY13	57,701	26.4	8,894	15.4	2,938	48.7	10.1	48.6	18.1	5.3	11.7
FY14E	68,967	19.5	12,561	18.2	5,746	95.6	19.7	95.6	9.3	15.3	15.9
FY15E	80,853	17.2	14,898	18.4	7,514	30.8	25.8	30.8	7.1	21.8	18.2

Figures in ₹ mn

eight injectables till date and is planning to launch four more in FY14E. Management expects the injectable business to contribute USD40 mn in FY14E and USD 60mn in FY15E. In addition, it plans to invest in an oncology injectable facility and split the injectable business into a strategic business unit.

Valuations

With new filings in Penems and high value injectables, we believe the company's pending approvals of 90 ANDAs auger well for quality of revenues from US generics and margin. While cost optimisation would boost margin, we are concerned on slow ramp-up in utilisation, strong outflow on capex and addition of new loan due to two new acquisitions. At CMP, the stock trades at 9.3x FY14E & 7.1x FY15E earnings. We initiate coverage on Aurobindo with 'BUY' recommendation and a target price of ₹ 258 (10x FY15E EPS).

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	45,647	57,701	68,967	80,853	Profit before tax	1,082	3,741	7,334	9,602
Other Operational income	626	853	900	1,000	Depreciation & w.o.	2,005	2,487	2,739	2,949
Income for Operations	46,274	58,553	69,867	81,853	Net Interest Exp	2,772	2,666	2,487	2,347
Total Expenditure	40,661	49,944	57,606	67,269	Direct taxes paid	888	(827)	(1,614)	(2,112)
Raw Material	25,198	29,908	34,584	40,926	Change in Working Capital	3,460	(10,094)	(2,534)	(5,360)
Employee Expenses	5,357	6,633	7,694	9,002	(A) CF from Opt. Activities	10,208	(2,026)	8,413	7,426
Other Expenses	10,107	13,403	15,328	17,341	Capex	(5,897)	(2,507)	(3,015)	(3,000)
EBIDTA (Excl. Other Income)	5,613	8,609	12,261	14,583	Free Cash Flow	4,311	(4,533)	5,399	4,426
Other Income	247	285	300	315	Inc./ (Dec.) in Investments	0	(163)	0	0
EBIDTA (Incl. Other Income)	5,860	8,894	12,561	14,898	(B) CF from Inv. Activities	(5,897)	(2,669)	(3,015)	(3,000)
Interest	2,772	2,666	2,487	2,347	Inc./ (Dec.) in Debt	1,585	8,115	(2,900)	(1,500)
Gross Profit	3,087	6,228	10,074	12,551	Interest exp net	(2,772)	(2,666)	(2,487)	(2,347)
Depreciation	2,005	2,487	2,739	2,949	Dividend Paid (Incl. Tax)	(415)	(519)	(649)	(811)
Profit Before Tax & EO Items	1,082	3,741	7,334	9,602	Other (bal fig.)	(3,882)	1,141	25	25
Extra Ordinary Exps/(Income)	0	1,634	1,368	0	(C) Cash Flow from Financing	(5,485)	6,071	(6,011)	(4,633)
Profit Before Tax	1,082	2,107	5,966	9,602	Net Change in Cash	(1,174)	1,376	(612)	(207)
Tax	(888)	827	1,614	2,112	Opening Cash balances	1,882	709	2,085	1,472
Net Profit	1,970	1,279	4,353	7,489	Closing Cash balances	709	2,085	1,472	1,265
Minority Interest	(6)	(25)	(25)	(25)	E-estimates				
Net Profit	1,976	1,304	4,378	7,514	IMPORTANT RATIOS				
Adj. Net Profit	1,976	2,938	5,746	7,514	Particulars	Mar12	Mar13	Mar14E	Mar15E
BALANCE SHEET					(A) Measures of Performance (%)				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Contribution Margin				
Sources of Funds					EBIDTA Margin (excl. O.I.)	12.3	14.9	17.8	18.0
Equity Capital	291	291	291	291	EBIDTA Margin (incl. O.I.)	12.8	15.4	18.2	18.4
Other Reserves	23,105	25,766	30,863	37,567	Interest / Sales	6.1	4.6	3.6	2.9
Net Worth	23,397	26,058	31,155	37,858	Gross Profit Margin	6.8	10.8	14.6	15.5
Minority Interest	102	110	110	110	Tax/PBT	(82.1)	39.3	27.0	22.0
Secured Loans	16,238	24,276	21,376	19,876	Net Profit Margin	4.3	2.3	6.3	9.3
Unsecured Loans	9,491	9,568	9,568	9,568	(B) As Percentage of Net Sales				
Loan Funds	25,728	33,844	30,944	29,444	Excise Duty % of Gross Sales	1.6	1.1	1.1	1.1
Deferred Tax Liability	(19)	680	680	680	Raw Material	55.2	51.8	50.1	50.6
Total Capital Employed	49,208	60,691	62,888	68,092	Employee Expenses	11.7	11.5	11.2	11.1
Applications of Funds					Other Expenses	22.1	23.2	22.2	21.4
Gross Block	30,863	37,635	40,635	43,635	(C) Measures of Financial Status				
Less: Accumulated Depreciation	8,916	11,246	13,985	16,935	Debt / Equity (x)	1.1	1.3	1.0	0.8
Net Block	21,947	26,389	26,649	26,700	Interest Coverage (x)	0.5	0.3	0.2	0.2
Capital Work in Progress	6,451	2,185	2,200	2,200	Average Cost Of Debt (%)	5.6	4.5	3.8	3.9
Investments	385	223	223	223	Debtors Period (days)	99	101	110	110
Current Assets, Loans & Advances					Closing stock (days)	124	122	70	71
Inventories	15,456	19,236	13,265	15,698	Inventory Turnover Ratio (x)	3.0	3.0	5.2	5.2
Sundry Debtors	12,400	15,970	20,785	24,367	Fixed Assets Turnover (x)	2.1	2.2	2.6	3.0
Cash and Bank Balance	709	2,085	1,472	1,265	Working Capital Turnover (x)	2.2	1.8	2.0	2.1
Loans and Advances	4,230	5,749	6,324	6,956	Non Cash Working Capital (₹ Mn)	19,717	29,810	32,344	37,704
Other Current Assets	743	943	943	943	(D) Measures of Investment				
<i>sub total</i>	33,536	43,982	42,789	49,228	EPS (₹) (excl EO)	6.8	10.1	19.7	25.8
Less : Current Liabilities & Provisions					CEPS (₹)	13.7	13.0	24.4	35.9
Current Liabilities	12,405	11,196	7,992	9,181	DPS (₹)	1.4	1.7	2.1	2.6
Provisions	706	891	980	1,078	Dividend Payout (%)	19.9	37.8	14.1	10.3
<i>sub total</i>	13,111	12,087	8,972	10,259	Profit Ploughback (%)	80.1	62.2	85.9	89.7
Net Current Assets	20,425	31,895	33,816	38,969	Book Value (₹)	80.4	89.5	107.0	130.0
Total Assets	49,208	60,691	62,888	68,092	RoANW (%)	8.3	5.3	15.3	21.8
E-estimates					RoACE (%)	7.8	11.7	15.9	18.2
					RoAIC (%) (Excl Cash & Invest.)	7.5	10.5	15.6	17.5
					(E) Valuation Ratios				
					CMP (₹)	183	183	183	183
					P/E (x)	26.9	18.1	9.3	7.1
					Market Cap. (₹ Mn.)	53,169	53,188	53,188	53,188
					MCap/ Sales (x)	1.2	0.9	0.8	0.7
					EV (₹ Mn.)	78,189	84,947	82,659	81,366
					EV/Sales (x)	1.7	1.5	1.2	1.0
					EV/EBDITA (x)	13.9	9.9	6.7	5.6
					P/BV (x)	2.3	2.0	1.7	1.4
					Dividend Yield (%)	0.7	0.9	1.2	1.4
					E-estimates				

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CMP: ₹ 339

Target Price: ₹ 399

Accumulate

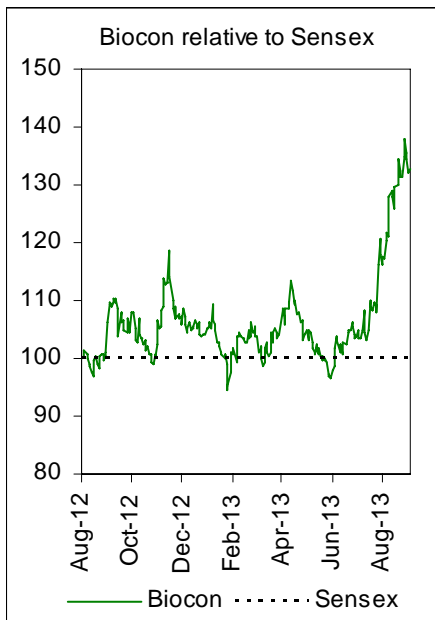
BSE Sensex	18,235
NSE Nifty	5,341

Scrip Details

Equity	₹ 1000mn
Face Value	₹ 5/-
Market Cap	₹ 68bn
	USD 1013mn
52 week High / Low	₹ 352 / 243
Avg. Volume (no)	976682
BSE Code	532523
NSE Symbol	BIOCON
Bloomberg Code	BIOS IN
Reuters Code	BION.BO

Shareholding Pattern as on June'13(%)

Promoter	52.15
FII's	14.85
MF/Banks/FIs	12.50
Public / Others	20.50



Clinical Gains....

Biocon has shifted its focus from statins to branded biotech formulations and contract research services. We estimate core Biopharma division to grow at 15% CAGR over FY13-15E with increasing contribution from domestic branded formulations and ramp up in fidaxomicin bulk supplies and Orlistat. The Mylan collaboration (products going off-patent 2015 onwards) is on track. We estimate 21% revenue CAGR in its CRO segment over FY13-15E with increased focus on integrated drug development services. Biocon has concluded second part of EU Phase III trial for biosimilar rh-Insulin and is currently compiling the data to be submitted to the European regulatory agencies. We have recently included Biocon in our preferred pick list.

Investment Rationale

Risk Adjusted Growth Strategy

Biocon is the only company which has made remarkable progress in the Indian Biotech industry with oncology and diabetes as its focus areas. Over the years, the company has entered into strategic partnerships and acquired IPR's in the diabetic space. The company is making efforts to move up the value chain through selective 505 (b) 2 & ANDA filings. We have recently included Biocon in our preferred picks list.

Biopharma Segment (76% of FY13 sales) – To sustain growth momentum

The branded formulations business is expected to grow by 18% CAGR during FY13-15E (FY13: ₹3.5bn) to ₹4.8bn. Ramp up in sales from Fidaxomicin supplies to Optimer will further add to the growth momentum. Moreover, product-development arrangement with Mylan (five biosimilar products, going off-patent 2015E onwards) is on track. We expect this division to grow at 15% CAGR over FY13-15E to ₹24.4bn.

Contract Research segment (23% of FY13 sales) – Gaining scale

The BMS contract (seven-year contract), with 450 FTE's, contributes 20-30% of Syngene sales. The company intends to gain scale in this vertical and shall consequently work out the modalities of getting Syngene listed. We expect CRO division to grow at 21% CAGR over FY13-15E to ₹7.4bn.

Financials

Year	Net Sales#	% Growth	EBIDTA	OPM %	Adj.PAT	% Growth	EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12#	20,865	(24.9)	5,173	24.8	3,384	(7.9)	16.9	(7.9)	20.1	15.7	16.2
FY13	24,853	19.1	5,430	21.8	3,069	(9.3)	15.3	(9.3)	22.1	12.4	14.9
FY14E	29,286	17.8	6,516	22.3	3,885	26.6	19.4	26.6	17.5	13.8	15.7
FY15E	33,797	15.4	7,672	22.7	4,693	20.8	23.5	20.8	14.5	15.1	16.7

Figures in ₹ mn, # Figures are ex-Axicorp

Commercialization of Rh-Insulin in regulated markets

Biocon has concluded second part of EU Phase III trial for biosimilar rh-Insulin aimed at establishing comparable immunogenicity and safety with the innovator products, over a 12 month evaluation period. The company is compiling the data and is in process of dossier submission with European regulatory authorities, thus paving the way for marketing authorization. Biocon is also contemplating harmonized filing for the insulin which could be used for both the US and EU markets.

Valuation

Revenue scale up in domestic branded business, Fidaxomicin bulk and Orlistat supplies, shall aid near-term revenue growth. Higher R&D costs (as the product pipeline advances) restricts margin expansion. At CMP, the stock trades at 17.5x FY14E and 14.5x FY15E earnings. We initiate with 'Accumulate' recommendation with a target price of ₹ 399 (17x FY15E EPS). We have also included Biocon in our preferred picks list.

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Income from Operations	20,865	24,853	29,286	33,797	Profit before tax	3,925	4,082	5,006	6,042
Other income	618	527	500	500	Depreciation & w.o.	1,744	1,793	1,900	2,000
Total Income	21,483	25,380	29,786	34,297	Net Interest Exp	122	81	110	130
Total Expenditure	15,692	19,423	22,770	26,125	Direct taxes paid	(541)	(975)	(1,101)	(1,329)
Operating Profit (excl. OI)	5,173	5,430	6,516	7,672	Chg. in Working Capital	1,949	(2,006)	(1,238)	(1,437)
Operating Profit (incl. OI)	5,791	5,956	7,016	8,172	(A) CF from Opt. Activities	7,199	2,975	4,677	5,406
Interest	122	81	110	130	Capex	(3,655)	(3,067)	(4,150)	(4,600)
Gross Profit	5,669	5,875	6,906	8,042	Free Cash Flow	3,544	(92)	527	806
Depreciation	1,744	1,793	1,900	2,000	(Inc)/ Dec. in Investments	(959)	(303)	0	0
Profit Before Tax & EO Items	3,925	4,082	5,006	6,042	Others (Bal Fig)	(15)	3,354	(572)	287
Extra Ordinary Exps/(Income)	0	(2,019)	0	0	(B) CF from Invnt. Activities	(4,629)	(16)	(4,722)	(4,313)
Profit Before Tax	3,925	6,102	5,006	6,042	Inc./ (Dec.) in Debt	(633)	(220)	2,012	1,250
Tax	541	975	1,101	1,329	Interest exp net	(122)	(81)	(110)	(130)
Net Profit	3,384	5,127	3,905	4,713	Dividend Paid (Incl. Tax)	(997)	(1,162)	(1,394)	(1,511)
Minority Interest	0	(38)	(20)	(20)	(C) CF from Financing	(1,752)	(1,463)	508	(391)
Net Profit After Minority Interest	3,384	5,088	3,885	4,693	Net Change in Cash	818	1,496	463	702
Net Profit After Minority Interest (w/o EO)	3,384	3,069	3,885	4,693	Opening Cash balances	4,415	5,233	6,729	7,192
					Closing Cash balances	5,233	6,729	7,192	7,894
					E-estimates				
BALANCE SHEET					IMPORTANT RATIOS				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Sources of Funds					(A) Measures of Performance (%)				
Equity Capital	1,000	1,000	1,000	1,000	Operating Profit Margin (excl. O.I.)	24.8	21.8	22.3	22.7
Reserves (excl Rev Res)	21,715	25,937	28,418	31,591	Operating Profit Margin (incl. O.I.)	27.8	24.0	24.0	24.2
Net Worth	22,715	26,937	29,418	32,591	Interest / Sales	0.6	0.3	0.4	0.4
Revaluation reserve	9	9	9	9	Gross Profit Margin	27.2	23.6	23.6	23.8
Minority Interest	38	653			Tax/PBT	13.8	16.0	22.0	22.0
Secured Loans	904	1,542	2,500	3,000	Net Profit Margin	16.2	12.3	13.3	13.9
Unsecured Loans	1,804	946	2,000	2,750					
Loan Funds	2,708	2,488	4,500	5,750	(B) Measures of Financial Status				
Deferred Tax Liability	(78)	412	632	898	Debt / Equity (x)	0.1	0.1	0.2	0.2
Total Capital Employed	25,392	30,499	34,560	39,249	Interest Coverage (x)	47.4	73.5	63.8	62.9
					Average Cost Of Debt (%)	4.0	3.1	3.1	2.5
Applications of Funds					Debtors Period (days)	86	75	86	87
Gross Block	20,354	24,556	28,610	33,260	Closing stock (days)	66	59	60	60
Less: Accumulated Depreciation	7,852	9,672	11,572	13,572	Inventory Turnover Ratio (x)	5.5	6.2	6.1	6.1
Net Block	12,502	14,884	17,038	19,688	Fixed Assets Turnover (x)	1.7	1.7	1.7	1.7
Capital Work in Progress	3,189	2,054	2,150	2,100	Working Capital Turnover (x)	7.2	3.9	3.6	3.3
Intangibles	1,235	1,290	1,400	1,350					
Investments	5,563	5,866	5,866	5,866	(C) Measures of Investment				
Current Assets, Loans & Advances					Earnings Per Share (₹) (excl EO)	16.9	15.3	19.4	23.5
Inventories	3,783	3,984	4,814	5,556	Earnings Per Share (₹)	16.9	25.4	19.4	23.5
Sundry Debtors	4,917	5,097	6,900	8,056	Cash Earnings Per Share (₹)	25.6	34.4	28.9	33.5
Cash and Bank Balance	5,233	6,729	7,192	7,894	Dividend Per Share (₹)	5.0	5.5	6.0	6.5
Loans and Advances	2,950	3,297	3,397	3,497	Dividend Payout (%)	29.6	21.6	30.9	27.7
Other Current Assets					Profit Ploughback (%)	70.4	78.4	69.1	72.3
<i>sub total</i>	16,883	20,067	22,303	25,002	Book Value (Rs.)	113.6	134.7	147.1	163.0
Less : Current Liabilities & Provisions					Return on Avg. Net Worth (%)	15.7	12.4	13.8	15.1
Current Liabilities	11,865	11,157	11,698	12,258	Return on Avg. Cap. Employed (%)	16.2	14.9	15.7	16.7
Provisions	2,115	2,505	2,500	2,500	Return on Cap. Employed (%)	27.7	23.3	23.8	24.2
<i>sub total</i>	13,980	13,662	14,198	14,758					
Net Current Assets	2,903	6,405	8,106	10,245	(D) Valuation Ratios				
Total Assets	25,392	30,499	34,560	39,249	CMP (₹)	339	339	339	339
E-estimates					PE (x)	20.1	22.1	17.5	14.5
					Market Cap (₹ Mn)	67,870	67,870	67,870	67,870
					Market Cap / Sales (x)	3.3	2.7	2.3	2.0
					EV (₹ Mn)	65,345	63,629	65,178	65,726
					EV/Sales (x)	3.1	2.6	2.2	1.9
					EV/EBDITA (x)	12.6	11.7	10.0	8.6
					P/BV (x)	3.0	2.5	2.3	2.1
					Dividend Yield (%)	1.5	1.6	1.8	1.9
					E-estimates				

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CMP: ₹ 642

Target Price: ₹ 727

Accumulate

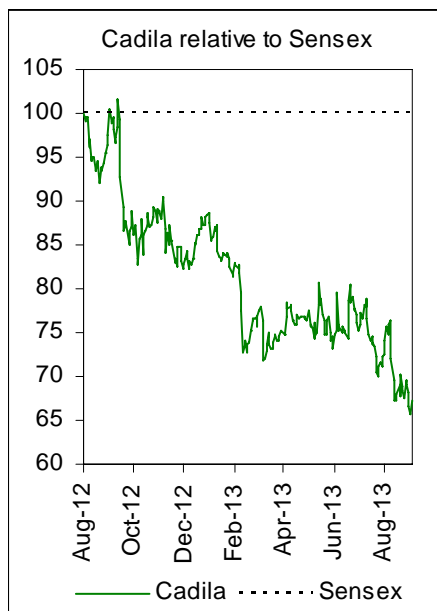
BSE Sensex	18235
NSE Nifty	5341

Scrip Details

Equity	₹ 1024mn
Face Value	₹ 5/-
Market Cap	₹ 131bn
	USD 1962mn
52 week High / Low	₹ 964 / 650
Avg. Volume (no)	130,367
BSE Code	532321
NSE Symbol	CADILAHC
Bloomberg Code	CDH IN
Reuters Code	CADI.BO

Shareholding Pattern as on June'13(%)

Promoter	74.79
FII's	5.42
MF/Banks/FIs	9.92
Public / Others	9.87



On a recovery mode

Cadila's (CDH) thrust on export formulations and contract manufacturing is well complemented with a strong domestic franchise. However, domestic formulations growth has been impacted on account of implementation of new pharma pricing policy. Also, lack of new product approvals and launch of authorized generics in the older product basket, has impacted the performance. CDH entered into several joint ventures (Hospira, Nycomed/Takeda, Bayer, Abbott) which has in turn positioned itself as a preferred contract manufacturer for Big Pharma companies. The JV biz has been impacted due to lack of new product approvals.

Investment Rationale

Domestic biz – Going through a rough patch

CDH has a 3.9% share and has a leading position in key therapies of CVS, gastro, women health care and respiratory (52% of the portfolio). However, in the near term domestic formulations growth has been impacted on account of destocking by stockists. The implementation of new pharma pricing policy would have an impact of ₹ 900mn on domestic formulation sales in FY14E. We estimate domestic formulation sales to record 13% CAGR over FY13-15E aided by incremental revenue contribution from Biochem and new launches.

Joint ventures – corrective measures to ramp-up the biz

The company has been proactive in identifying and capitalizing on partnership opportunities since FY07, signed the Nycomed JV - one of the most profitable JV by an Indian player (70%+ net margin) to manufacture pantoprazole intermediates. With increasing genericisation of Protonix, the company offset the loss in sales through Hospira JV (oncology injectables) and currently sells six products in EU & three in US under this arrangement. However, the JV biz has been impacted due to lack of new product approvals. Corrective measures taken by the company are: a) Hospira JV: The company has added a new line and expects sales to pick-up in FY15E b) Takeda/ Nycomed JV: The company is in advanced talks for adding new products and expects to finalize by end of FY14E and c) Bayer JV: Growth would be on account of launch of patented products in FY14E.

Financials

Year	Net Sales#	% Growth	EBIDTA	OPM %	Adj.PAT	% Growth	EPS (₹)*	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12	52,633	13.7%	10,839	20.6%	7,306	3.9%	35.7	3.9%	18.0	27.5	23.0
FY13	63,581	20.8%	11,257	17.7%	6,553	-10.3%	32.0	-10.3%	20.1	23.5	17.5
FY14E	69,709	9.6%	12,199	17.5%	7,302	11.4%	35.7	11.4%	18.0	22.5	16.6
FY15E	81,864	17.4%	14,736	18.0%	9,299	27.4%	45.4	27.4%	14.1	24.4	18.9

Figures in ₹ mn, # Includes Other Operating Income, * Adjusted for exceptional items

Export formulations -

The company's export formulations business has grown at 31% CAGR over last five years, through its distribution tie-ups, complex product filings and cost competencies (back-ended domestic manufacturing). In the near term, growth has been impacted on account of lack of new product approvals and launch of authorized generics in their older product basket (impacting the margins). The company expects 5-8 new product approvals in FY14 (compared to earlier guidance of 20+ approvals). The company expects to grow by 20% in FY15E led by 10-15 new product approvals. We estimate this division to grow by 15% CAGR over FY13-15E.

Valuations

We believe that FY14 will be a year of recovery for CDH. We estimate a strong 19% EPS CAGR for FY13 -15E with RoCE and RoE in the range of 19-20% and 24-25% in FY14E/15E respectively. The stock trades at 18.0x FY14E and 14.1x FY15E consolidated EPS. We remain positive on the long term prospects of the company and initiate coverage with 'Accumulate' with a target price of ₹ 727 (16x FY15E EPS).

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	50,900	61,554	67,609	79,764	Profit before tax	7,942	8,112	9,031	11,470
Operating Income	1,733	2,027	2,100	2,100	Depreciation & w.o.	1,579	1,828	2,150	2,400
Net Sales/Income From Opet.	52,633	63,581	69,709	81,864	Net Interest Exp	1,849	1,686	1,518	1,366
Non Operating Income	532	370	500	500	Direct taxes paid	(1,130)	(1,195)	(1,355)	(1,720)
Total Income	53,165	63,951	70,209	82,364	Chg. in Working Capital	(3,930)	(4,998)	(1,374)	(4,067)
Total Expenditure	41,795	52,324	57,510	67,129	Other	(17)	(17)	(17)	(17)
Raw Material	16,794	23,204	25,095	29,062	(A) CF from Opt. Activities	6,292	5,416	9,953	9,431
Employee Expenses	7,512	9,032	10,108	11,870	Capex	(12,397)	(6,500)	(6,500)	(4,500)
Other Expenses	17,489	20,088	22,307	26,197	Free Cash Flow	(6,105)	(1,084)	3,453	4,931
EBIDTA (Excl. Other Income)	10,839	11,257	12,199	14,736	(Inc)/ Dec. in Investments	(35)	0	0	0
EBIDTA (Incl. Other Income)	11,370	11,627	12,699	15,236	Others (Bal Fig)	(123)	256	288	362
Interest	1,849	1,686	1,518	1,366	(B) CF from Invnt. Activities	(12,555)	(6,244)	(6,212)	(4,138)
Gross Profit	9,521	9,941	11,181	13,870	Issue of Equity/ Preference	(116)	0	0	0
Depreciation	1,579	1,828	2,150	2,400	Inc./(Dec.) in Debt	11,977	5,599	(1,350)	(2,000)
Profit Before Tax & EO Items	7,942	8,112	9,031	11,470	Interest exp net	(1,849)	(1,686)	(1,518)	(1,366)
Profit Before Tax	7,942	8,112	9,031	11,470	Dividend Paid (Incl. Tax)	(2,066)	(2,203)	(2,479)	(3,029)
Tax	1,130	1,195	1,355	1,720	(C) CF from Financing	7,946	1,709	(5,346)	(6,395)
Reported Net Profit	6,812	6,917	7,677	9,749	Net Change in Cash	1,683	881	(1,606)	(1,103)
Adjustments on consolidation	286	364	375	450	Opening Cash balances	2,952	4,635	5,517	3,911
Net Profit	6,526	6,553	7,302	9,299	Closing Cash balances	4,635	5,517	3,911	2,808
Extraordinary & Forex Items	780	0	0	0	E-estimates				
Adjusted Net Profit	7,306	6,553	7,302	9,299					

BALANCE SHEET					IMPORTANT RATIOS				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Sources of Funds					(A) Measures of Performance (%)				
Equity Capital	1,024	1,024	1,024	1,024	Contribution Margin				
Other Reserves	24,712	29,062	33,885	40,155	EBIDTA Margin (excl. O.I.)	20.6	17.7	17.5	18.0
Net Worth	25,736	30,086	34,909	41,178	EBIDTA Margin (incl. O.I.)	21.4	18.2	18.1	18.5
Secured Loans	13,655	18,600	17,600	16,600	Interest / Sales	3.6	2.7	2.2	1.7
Unsecured Loans	9,296	9,950	9,600	8,600	Gross Profit Margin	17.9	15.5	15.9	16.8
Loan Funds	22,951	28,550	27,200	25,200	Tax/PBT	14.2	14.7	15.0	15.0
Deferred Tax Liability	1,185	1,424	1,695	2,039	Net Profit Margin	13.7	10.2	10.4	11.3
Minority Interest	904	1,268	1,643	2,093					
Total Capital Employed	50,776	61,328	65,447	70,511	(B) As Percentage of Net Sales				
					Raw Material	31.9	36.5	36.0	35.5
Applications of Funds					Employee Expenses	14.3	14.2	14.5	14.5
Gross Block	40,229	48,314	54,814	60,814	Other Expenses	33.2	31.6	32.0	32.0
Less: Accumulated Depreciation	11,750	13,578	15,728	18,128					
Net Block	28,479	34,736	39,086	42,686	(C) Measures of Financial Status				
Capital Work in Progress	5,085	3,500	3,500	2,000	Debt / Equity (x)	0.9	0.9	0.8	0.6
Investments	242	242	242	242	Interest Coverage (x)	6.1	6.9	8.4	11.2
Current Assets, Loans & Advances					Average Cost Of Debt (%)	10.9	6.5	5.4	5.2
Inventories	10,905	13,491	14,078	16,608	Debtors Period (days)	64	65	64	64
Sundry Debtors	8,863	10,962	11,855	13,986	Closing stock (days)	78	80	76	76
Cash and Bank Balance	4,635	5,517	3,911	2,808	Inventory Turnover Ratio (x)	4.7	4.6	4.8	4.8
Loans and Advances	5,131	6,631	7,631	8,631	Fixed Assets Turnover (x)	1.3	1.3	1.2	1.3
Other Current Assets	421	505	606	727	Working Capital Turnover (x)	3.0	2.7	3.0	3.1
<i>sub total</i>	<i>29,955</i>	<i>37,106</i>	<i>38,081</i>	<i>42,761</i>	Non Cash Working Capital (₹ Mn)	12,335	17,333	18,708	22,775
Less : Current Liabilities & Provisions									
Current Liabilities	9,948	10,552	11,483	12,649	(D) Measures of Investment				
Provisions	3,037	3,703	3,979	4,529	Adj. EPS (₹) (excl EO)	35.7	32.0	35.7	45.4
<i>sub total</i>	<i>12,985</i>	<i>14,256</i>	<i>15,462</i>	<i>17,178</i>	EPS (₹)	31.9	32.0	35.7	45.4
Net Current Assets	16,970	22,850	22,619	25,583	CEPS (₹)	43.4	40.9	46.2	57.1
Total Assets	50,776	61,328	65,447	70,511	DPS (₹)	7.5	8.0	9.0	11.0
E-estimates					Dividend Payout (%)	23.5	25.0	25.2	24.2
					Profit Ploughback (%)	76.5	75.0	74.8	75.8
					Book Value (₹)	125.7	146.9	170.5	201.1
					RoANW (%)	27.5	23.5	22.5	24.4
					RoACE (%)	23.0	17.5	16.6	18.9
					RoAIC (%) (Excl Cash & Invest.)	25.2	19.2	18.0	19.9
					(E) Valuation Ratios				
					CMP (₹)	642	642	642	642
					P/E (x)	18.0	20.1	18.0	14.1
					Market Cap. (₹ Mn.)	131,449	131,449	131,449	131,449
					MCap/ Sales (x)	2.5	2.1	1.9	1.6
					EV (₹ Mn.)	149,765	154,482	153,737	151,841
					EV/Sales (x)	2.8	2.4	2.2	1.9
					EV/EBDITA (x)	13.8	13.7	12.6	10.3
					P/BV (x)	5.1	4.4	3.8	3.2
					Dividend Yield (%)	1.2	1.2	1.4	1.7
					E-estimates				

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CMP: ₹ 406

Target Price: ₹ 480

Accumulate

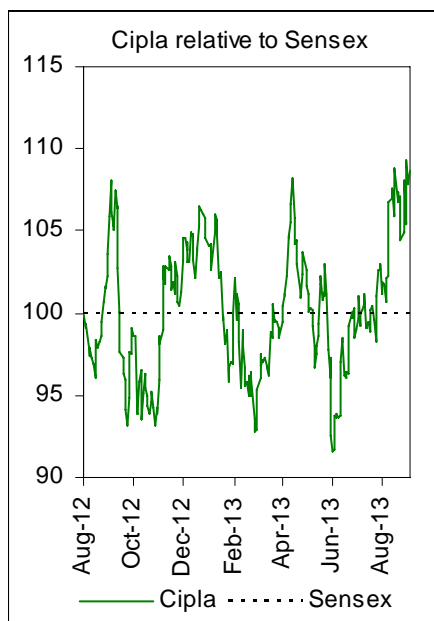
BSE Sensex	18,235
NSE Nifty	5,341

Scrip Details

Equity	₹ 1606mn
Face Value	₹ 2/-
Market Cap	₹ 326bn
	USD 4862mn
52 week High / Low	₹ 435 / 350
Avg. Volume (no)	1454719
BSE Code	500087
NSE Symbol	CIPLA
Bloomberg Code	CIPLA IN
Reuters Code	CIPL.BO

Shareholding Pattern as on June'13(%)

Promoter	36.80
FII's	23.11
MF/Banks/FIs	10.81
Public / Others	29.28



On a Transformation Path...

Cipla has outperformed market growth over the past five years (CAGR of 13.1% over FY08-13) and has consistently improved its market share. Cipla's large manufacturing infrastructure, strong chemistry skills and huge inhaler capacity make it a partner of choice for global MNCs that are ramping up their generics presence in emerging markets. This, along with its low-risk strategy and a strong capex (currently underutilized) should ensure good long-term potential. We believe Cipla has one of the strongest generic pipelines among Indian companies. After a long delay, we believe Cipla's CFC-free inhaler pipeline is likely to be gradually commercialized in Europe and upsides from high-margin opportunities like Seretide can potentially come through over the next two years.

Investment Rationale

Domestic formulations

The top four therapeutic segments - respiratory, anti-infectives, CVS and gynecology segments, contribute ~70% of Cipla's domestic formulation revenue. Cipla is the market leader in two of the largest therapy segments, anti-infectives and respiratory segments, though dependence on anti-infectives has fallen over the years. Cipla derives 58% of its revenue from acute therapies and the rest from chronic therapeutic areas. Cipla's sizable presence in these segments makes it an attractive play in the domestic formulations business. We expect Cipla's domestic formulations business to post 14% CAGR over FY13-15E, led by one of the largest field forces and new launches but might get impacted by 2-3% on account of new pharma pricing policy.

CFC-free inhalers a key long-term trigger

Cipla is developing eight inhalers and has the third largest inhaler manufacturing capacity globally. It has commercialized some of its inhalers in the UK, Germany, Spain and Portugal. While the launch of these inhalers is a key long-term trigger, the visibility of launch timelines is poor. The management expects its range of eight inhalers to be commercialized in Europe over the next 2-3 years and it expects 3-6 players for each product in this category, implying that this will be a low-competition, high-margin opportunity.

Financials

Year	Net Sales	% Growth	EBIDTA	OPM %	Adj.PAT	% Growth	EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12	68,477	12.0	17,262	25.2	10,769	11.1	13.4	11.1	30.3	16.0	19.4
FY13	80,154	17.1	21,193	26.4	15,073	40.0	18.8	40.0	21.6	18.1	22.5
FY14E	92,240	15.1	24,144	26.2	16,797	11.4	20.9	11.4	19.4	17.3	20.6
FY15E	104,949	13.8	27,609	26.3	19,212	14.4	23.9	14.4	17.0	17.1	20.7

Figures in ₹ mn

Developed markets – Moving away from partnership model

In the developed markets, Cipla is building its own front-end operations for selling generic medicines through its own distribution network rather than supplying it through its partners. We believe this strategy to yield higher margins going ahead.

Valuation

We believe Cipla has one of the strongest generic pipelines among Indian companies. After a long delay, we believe Cipla's CFC-free inhaler pipeline is likely to be gradually commercialized in Europe and upsides from high-margin opportunities like Seretide can potentially come through over the next two years. We estimate EPS CAGR at 17% over FY13-15 with potential upsides from MNC supplies and CFC-free inhalers. The growth will be led by 13% CAGR for the international business, tempered by reducing technology licensing income. At CMP, the stock trades at 19.4x FY14E & 17.0x FY15E earnings. We initiate coverage on Cipla with 'Accumulate' recommendation and a target price of ₹ 480 (20x FY15E EPS).

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	68,477	81,154	92,240	104,949	Profit before tax	14,478	24,469	21,854	25,004
Other Operational income	1,730	1,871	1,760	1,760	Depreciation & w.o.	3,122	3,380	3,984	4,261
Income for Operations	70,207	82,025	94,000	106,709	Net Interest Exp	383	384	200	210
Total Expenditure	52,945	60,832	69,762	79,634	Direct taxes paid	(3,065)	(5,148)	(5,088)	(5,822)
Raw Material	27,393	30,629	35,664	40,553	Chg. in Working Capital	4,455	(6,636)	(3,500)	(5,690)
Employee Expenses	7,725	9,693	10,783	12,484	(A) CF from Opt. Activities	19,374	16,450	17,451	17,962
Manufacturing & Other Expenses	17,827	20,510	23,315	26,597	Capex	(4,719)	(6,975)	(5,000)	(5,000)
EBIDTA (Excl. Other Income)	17,262	21,193	24,144	27,069	Free Cash Flow	14,655	9,475	12,451	12,962
Other Income	722	2,291	2,440	2,450	Inc./ (Dec.) in Investments	(6,783)	(12,633)	324	(1,000)
EBIDTA (Incl. Other Income)	17,984	23,484	26,584	30,059	(B) CF from Inv. Activities	(11,502)	(19,609)	(4,676)	(6,000)
Interest	383	334	300	286	Inc./ (Dec.) in Debt	(5,584)	9,535	0	0
Gross Profit	17,600	23,150	26,284	29,773	Interest exp net	(383)	(384)	(200)	(210)
Depreciation	3,122	3,030	3,984	4,261	Dividend Paid (Incl. Tax)	(1,866)	(2,342)	(2,810)	(3,279)
Profit Before Tax & EO Items	14,478	20,120	22,301	25,512	Other (bal fig.)	(92)	(3,125)	(345)	(370)
Profit Before Tax	14,478	20,120	22,301	25,512	(C) CF from Financing	(7,926)	3,684	(3,355)	(3,859)
Tax	3,065	5,048	5,533	6,330	Net Change in Cash	(55)	526	9,420	8,104
Net Profit	11,413	15,073	16,767	19,182	Opening Cash balances	960	905	1,430	10,850
Minority Interest	(29)	0	(30)	(30)	Closing Cash balances	905	1,430	10,850	18,954
Net Profit	11,442	15,073	16,797	19,212	E-estimates				
Adj.Net Profit	10,769	15,073	16,797	19,212					

BALANCE SHEET				
Particulars	Mar12	Mar13	Mar14E	Mar15E
Sources of Funds				
Equity Capital	1,606	1,606	1,606	1,606
Share Premium	14,290	14,290	14,290	14,290
Other Reserves	60,494	74,291	88,278	104,212
Net Worth	76,389	90,187	104,173	120,107
Secured Loans	33	6	6	6
Unsecured Loans	102	9,664	9,664	9,664
Loan Funds	135	9,669	9,669	9,669
Deferred Tax Liability	2,332	2,805	2,805	2,805
Total Capital Employed	78,856	102,662	116,648	132,582
Applications of Funds				
Gross Block	46,266	53,279	57,279	61,279
Less: Accumulated Depreciation	14,111	17,076	20,684	24,545
Net Block	32,155	36,203	36,595	36,734
Capital Work in Progress	3,712	3,674	4,674	5,674
Investments	12,691	25,324	25,000	26,000
Current Assets, Loans & Advances				
Inventories	18,501	23,871	25,271	28,753
Sundry Debtors	15,536	16,688	19,967	22,718
Cash and Bank Balance	905	1,430	10,850	18,954
Loans and Advances	9,405	9,313	10,313	11,313
Other Current Assets	594	74	74	74
<i>sub total</i>	44,940	51,376	66,474	81,811
Less : Current Liabilities & Provisions				
Current Liabilities	12,117	11,093	12,989	14,222
Provisions	2,525	2,824	3,106	3,417
<i>sub total</i>	14,642	13,916	16,095	17,638
Net Current Assets	30,299	37,460	50,379	64,173
Total Assets	78,856	102,662	116,648	132,582
E-estimates				

IMPORTANT RATIOS				
Particulars	Mar12	Mar13	Mar14E	Mar15E
(A) Measures of Performance (%)				
Contribution Margin				
EBIDTA Margin (excl. O.I.)	24.6	31.5	25.8	25.4
EBIDTA Margin (incl. O.I.)	25.6	34.2	27.7	27.6
Interest / Sales	0.6	0.5	0.2	0.2
Gross Profit Margin	25.1	33.8	27.5	27.4
Tax/PBT	21.2	21.0	23.3	23.3
Net Profit Margin	16.3	23.5	17.9	18.0
(B) As Percentage of Net Sales				
Excise Duty % of Gross Sales	1.6	1.3	1.3	1.3
Raw Material	40.0	31.4	38.7	38.6
Employee Expenses	11.3	12.6	11.7	11.9
Other Expenses	26.0	26.1	25.3	25.3
(C) Measures of Financial Status				
Debt / Equity (x)	0.0	0.1	0.1	0.1
Interest Coverage (x)	46.9	73.6	130.2	140.4
Average Cost Of Debt (%)	13.1	7.8	2.1	2.2
Debtors Period (days)	83	76	79	79
Closing stock (days)	99	108	100	100
Inventory Turnover Ratio (x)	3.7	3.4	3.7	3.7
Fixed Assets Turnover (x)	1.5	1.5	1.6	1.7
Working Capital Turnover (x)	2.3	2.2	1.8	1.6
Non Cash Working Capital (₹ Mn)	29,394	36,029	39,529	45,219
(D) Measures of Investment				
EPS (₹) (excl EO)	13.4	24.1	20.9	23.9
EPS (₹)	14.3	24.1	20.9	23.9
CEPS (₹)	18.1	28.3	25.9	29.2
DPS (₹)	2.0	2.5	3.0	3.5
Dividend Payout (%)	14.0	10.4	14.3	14.6
Profit Ploughback (%)	86.0	89.6	85.7	85.4
Book Value (₹)	95.1	112.3	129.7	149.6
RoANW (%)	16.0	23.2	17.3	17.1
RoACE (%)	19.4	27.4	20.1	20.2
RoAIC (%) (Excl Cash & Invest.)	19.6	27.7	21.3	23.0
(E) Valuation Ratios				
CMP (₹)	406	406	406	406
P/E (x)	28.5	21.6	19.4	17.0
Market Cap. (₹ Mn.)	325,777	325,777	325,777	325,777
MCap/ Sales (x)	4.8	4.1	3.5	3.1
EV (₹ Mn.)	325,007	334,016	324,613	316,512
EV/Sales (x)	4.7	4.2	3.5	3.0
EV/EBDITA (x)	18.8	15.8	13.4	11.5
P/BV (x)	4.3	3.6	3.1	2.7
Dividend Yield (%)	0.5	0.6	0.7	0.9
E-estimates				

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CMP: ₹ 956

Target Price: ₹ 1141

Accumulate

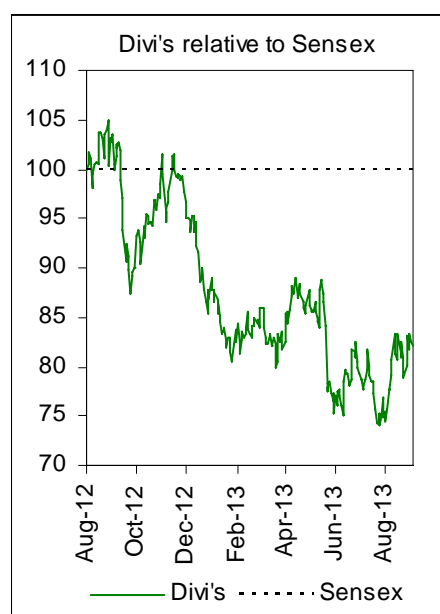
BSE Sensex	18235
NSE Nifty	5341

Scrip Details

Equity	₹ 265mn
Face Value	₹ 2/-
Market Cap	₹ 127bn
	USD 1894mn
52 week High / Low	₹ 1233 / 905
Avg. Volume (no)	194116
BSE Code	532488
NSE Symbol	DIVISLAB
Bloomberg Code	DIVI IN
Reuters Code	DIVI.BO

Shareholding Pattern as on June'13(%)

Promoter	52.15
FII's	14.85
MF/Banks/FIs	12.50
Public / Others	20.50



The Art Of Synthesis...

Divi's Laboratories (Divi's) has positioned itself as India's leading player in CRAMs segment. We like its focus on high value low competition products. Its key business segments viz. Custom synthesis (CS) & APIs (95% of sales) is expected to register 18% CAGR over FY13-15E. Divi's is one of the few CRAMs players that have refrained from entering the formulation space, to demonstrate its strict adherence to IP policies. This is a reason in itself for its large MNC clientele (20 innovators) to grow their relationship with Divi's.

The CS division is expected to be the major growth driver led by ramp up in new Vizag SEZ operations and increased order inflows. The API segment is expected to sustain growth as it leverages on selective patent expirations in US. Gradual scale up in its carotenoids portfolio shall aid overall growth momentum. We estimate 19.1% CAGR in revenue over FY13-15E aided by turnaround in the CRAMs industry.

Investment Rationale

Strong chemistry skills to drive growth and check competition

Divi's has marked its presence in the CS business through effective demonstration of its inherent chemistry skill sets. This has consequently translated into strong relationships with major pharma MNCs. Further, the company has kept itself from entering the formulation business, adding comfort to its clients. Revenue contribution from this segment declined in FY10 in line with the overall slowdown in CRAM industry. But we anticipate this business to witness high growth in near future on account of increasing cost-pressure faced by innovator companies and low R&D productivity. We expect the CS division to grow by 20.5% CAGR over FY13-15E, led by increased capacity utilization at Vizag SEZ, post the USFDA inspection and increased order inflows.

A lean portfolio of APIs to provide stable growth

We believe Divi's strategy to focus only on high-yielding API products positions it as the dominant supplier to the innovators. Notably, Divi's maintains dominant market share of 70% in Naproxene and Dextromethorphan. The company currently has 41 DMF filings and plans to add 3-4 filings every year going forward. Further aided by increased genericization of pharma markets of US and Europe, we believe revenue from APIs to grow by 18% CAGR over FY13-15E.

Financials

Year	Net Sales#	% Growth	EBIDTA	OPM %	Adj.PAT	% Growth	EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12	18,640	41.6	6,904	37.0	5,333	24.2	40.2	24.2	24.7	27.1	33.2
FY13	21,448	15.1	7,132	33.3	5,000	-6.2	37.7	-6.2	26.3	22.1	28.7
FY14E	25,370	18.3	9,894	39.0	7,453	49.1	56.1	49.1	17.6	28.1	35.3
FY15E	29,907	17.9	11,649	39.0	8,912	19.6	67.1	19.6	14.8	27.8	35.2

Figures in ₹mn, # - includes other operating income

Increasing contribution from carotenoids adding to growth momentum

The global market for carotenoids is estimated at USD 1bn and is dominated by DSM and BASF with 60% combined share. Carotenoids contribute 4% of Divi's total sales in FY13. The company has created an extensive portfolio of carotenoids like Astaxanthin, Canathaxanthin, Apocarotenal. We expect the segment sales to reach ₹1.3bn in FY15E and contribute 5% of the total sales, aided by gradual volume off-take.

Valuation

We expect 19% revenue growth over FY13-15E mainly led by increased order flows and ramp up in its new facility at Vizag SEZ (translates into higher operating leverage). Debt free balance sheet and controlled capex enables Divis to generate healthy cash flows which in turn reflects in its high return ratios. At CMP, the stock trades at 17.0x FY14E and 14.2x FY15E earnings. We initiate coverage on Divi's Laboratories with a 'Accumulate' recommendation and a target price of ₹ 1141 (17x FY15E EPS).

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	18,586	21,399	25,320	29,857	Profit before tax and EOI	6,806	6,792	9,679	11,574
Other Operational income	54	49	50	50	Depreciation & w.o.	621	770	930	1,040
Income from Operations	18,640	21,448	25,370	29,907	Net Interest Exp	37	18	35	35
Other Income	561	448	750	1,000	Direct taxes paid	(1,474)	(1,792)	(2,226)	(2,662)
Total Income	19,201	21,897	26,120	30,907	Change in Working Capital	(1,441)	(1,223)	(2,782)	(3,254)
Total Expenditure	11,736	14,317	15,476	18,258	(A) CF from Opt. Activities	4,550	4,564	5,636	6,733
EBIDTA (Excl. Other Income)	6,904	7,132	9,894	11,649	Capex	(3,264)	(1,906)	(500)	(1,300)
EBIDTA (Incl. Other Income)	7,465	7,580	10,644	12,649	Free Cash Flow	1,286	2,658	5,136	5,433
Interest	37	18	35	35	Inc./ (Dec.) in Investments	486	(730)	(1,500)	(3,000)
Gross Profit	7,427	7,562	10,609	12,614	(B) CF from Inv. Activities	(2,775)	(2,641)	(2,000)	(4,300)
Depreciation	621	770	930	1,040	Issue of Equity/ Preference	76	(76)	0	0
Profit Before Tax & EO Items	6,806	6,792	9,679	11,574	Inc./ (Dec.) in Debt	324	(149)	(25)	0
Tax	1,474	1,792	2,226	2,662	Interest exp net	(37)	(18)	(35)	(35)
Net Profit	5,333	5,000	7,453	8,912	Dividend Paid (Incl. Tax)	(2,005)	(2,237)	(2,468)	(2,854)
BALANCE SHEET					(C) CF from Fin. Activities	(1,643)	(2,480)	(2,528)	(2,889)
Particulars	Mar12	Mar13	Mar14E	Mar15E	Net Change in Cash	133	(557)	1,108	(456)
Sources of Funds					Opening Cash balances	177	309	(242)	865
Equity Capital	265	265	265	265	Closing Cash balances	309	(242)	865	410
Share Premium	1,041	965	965	965	E-estimates				
Other Reserves	20,009	22,772	27,757	33,815	IMPORTANT RATIOS				
Net Worth	21,315	24,003	28,987	35,045	Particulars	Mar12	Mar13	Mar14E	Mar15E
Secured Loans	527	375	350	350	(A) Measures of Performance (%)				
Unsecured Loans	27	30	30	30	Contribution Margin				
Loan Funds	554	405	380	380	EBIDTA Margin (excl. O.I.)	37.0	33.3	39.0	39.0
Net Deferred Tax Liability	609	609	609	609	EBIDTA Margin (incl. O.I.)	40.0	35.3	42.0	42.3
Total Capital Employed	22,479	25,016	29,976	36,034	Interest / Sales	0.2	0.1	0.1	0.1
Applications of Funds					Gross Profit Margin	40.0	35.3	41.9	42.2
Goodwill On Consolidation					Tax/PBT	21.7	26.4	23.0	23.0
Gross Block	10,921	12,921	15,121	16,621	Net Profit Margin	28.6	23.3	29.4	29.8
Less: Accumulated Depreciation	3,536	4,306	5,236	6,276	(B) As Percentage of Net Sales				
Net Block	7,384	8,615	9,885	10,345	Raw Materials Consumed	41.4	42.0	38.3	38.3
Capital WIP	1,816	2,400	700	500	(Increase)/Decrease in Stocks	(0.5)	0.0	0.0	0.0
Unallocated Exp. pending allocation	4	0	0	0	Employees Cost	8.1	9.2	8.7	9.0
Advances for Capital Works	674	0	0	0	Other Expenses	14.0	15.5	14.0	13.8
Investments	4,770	5,500	7,000	10,000	(C) Measures of Financial Status				
Current Assets, Loans & Advances					Interest Coverage (x)	199.6	425.8	304.1	361.4
Inventories	6,790	7,856	9,712	11,861	Average Cost Of Debt (%)	9.5	3.7	8.9	9.2
Sundry Debtors	4,980	5,745	6,937	8,589	Debtors Period (days)	98	98	100	105
Cash and Bank Balance	309	(242)	865	410	Closing stock (days)	133	134	140	145
Loans and Advances	834	1,000	1,200	1,500	Creditor (days)	135.5	133.0	130.0	125.0
Other Current Assets	5	5	5	5	Inventory Turnover Ratio (x)	2.7	2.7	2.6	2.5
<i>sub total</i>	12,918	14,364	18,719	22,364	Fixed Assets Turnover (x)	1.7	1.7	1.7	1.8
Less : Current Liabilities & Provisions					Working Capital Turnover (x)	2.4	2.5	2.0	2.0
Current Liabilities	2,989	3,535	3,764	4,226	Non Cash Working Capital (₹ Mn)	7,521	8,744	11,526	14,780
Provisions	2,099	2,327	2,563	2,949	(D) Measures of Investment				
<i>sub total</i>	5,088	5,862	6,327	7,175	EPS (₹)	40.2	37.7	56.1	67.1
Net Current Assets	7,830	8,502	12,392	15,189	CEPS (₹)	44.9	43.5	63.2	75.0
Total Assets	22,479	25,016	29,976	36,034	DPS (₹)	13.0	14.5	16.0	18.5
E-estimates					Dividend Payout (%)	32.4	38.5	28.5	27.6
					Profit Ploughback (%)	67.6	61.5	71.5	72.4
					Book Value (₹)	160.6	180.8	218.4	264.0
					RoANW (%)	27.1	22.1	28.1	27.8
					RoACE (%)	33.2	28.7	35.3	35.2
					RoAIC (%) (Excl Cash & Invest.)	33.6	28.7	35.7	35.9
					(E) Valuation Ratios				
					CMP (₹)	956	956	956	956
					P/E (x)	23.8	25.4	17.0	14.2
					Market Cap. (₹ Mn.)	126,901	126,901	126,901	126,901
					MCap/ Sales (x)	6.8	5.9	5.0	4.3
					EV (₹ Mn.)	127,146	127,548	126,416	126,871
					EV/Sales (x)	6.8	6.0	5.0	4.2
					EV/EBDITA (x)	18.4	17.9	12.8	10.9
					P/BV (x)	6.0	5.3	4.4	3.6
					Dividend Yield (%)	1.4	1.5	1.7	1.9
					E-estimates				

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CMP: ₹ 2210

Target Price: ₹ 2382

Accumulate

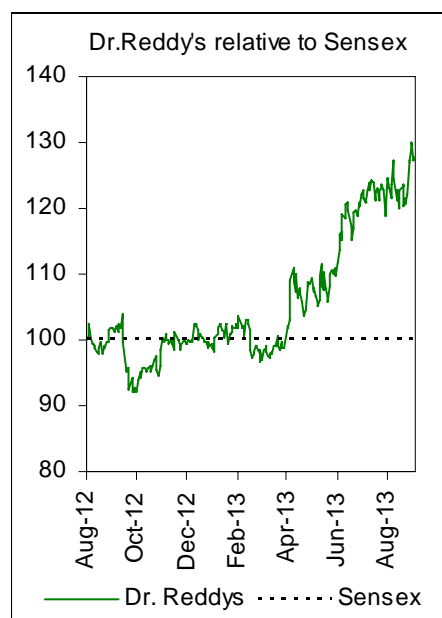
BSE Sensex	18235
NSE Nifty	5341

Scrip Details

Equity	₹ 849mn
Face Value	₹ 5/-
Market Cap	₹ 375bn
	USD 5602mn
52 week High / Low	₹ 2401 / 1617
Avg. Volume (no)	453415
BSE Code	500124
NSE Symbol	DRREDDY
Bloomberg Code	DRRD IN
Reuters Code	REDY.BO

Shareholding Pattern as on June'13(%)

Promoter	25.53
FII's	32.69
MF/Banks/FIs	8.84
Public / Others	32.94



US Dose for Healthy Future...

Dr. Reddy's Laboratories (DRL) continues to build upon its generics capability on selective niche products and biosimilars. The company's key strength lays in its complex chemistry skills supported by a captive mine of APIs, making it a dominant player in the global generics market. Recent launches (gPropecia, gDacogen, gReclast, gPropecia) with limited competition shall add fuel to the base business growth momentum. DRL has gained traction in biosimilars in emerging markets and is gearing itself for the next wave of opportunity in the regulated markets (2014E onwards)

Investment Rationale

US biz- focusing on niche and complex therapies

We anticipate US generics segment (30% of sales) to be the key growth driver in the near future. The company is focusing on complex molecules and therapies including dermatology and injectables which offer strong visibility in the long term. In the near term, growth would be supported by recent launches such as gDacogen, gReclast, gToprol XL and niche opportunities such as gVidaza, gAccutane, gXeloda and gAvelox. The company has 65 ANDAs pending approval, of which 38 are Para IVs and 8 FTF opportunities. We estimate US sales to register USD 870mn in FY14E and USD 930mn in FY15E.

Emerging markets - growth to driven by in-licensing/partnership arrangements

We expect DRL's formulation exports to emerging markets to record 18% CAGR over FY13-15E led by a) Russian OTC market- addition of more products and in-licensing arrangements to expand its product portfolio, b) ramp-up in revenues from partnership arrangement in emerging markets.

Domestic formulations – multiple growth challenges persist

DRL's domestic formulation business is impacted by low volume off take due to implementation of new pricing policy and trade strike in Maharashtra. As per company, new pricing policy would have an impact of ₹ 550mn on domestic sales. Going ahead, company expects to grow in-line with market growth rate (12-14%). However, we expect the revival process to be gradual and have estimated 10% CAGR over FY13-15E.

Financials

Year	Net Sales#	% Growth	EBIDTA	OPM %	Adj.PAT*	% Growth Adj. EPS (₹)	% Growth PER (x)	ROANW(%)	ROACE (%)
FY12	97,502	28.6	24,506	25.1	12,533	12.9	74	29.9	24.2
FY13	118,745	21.8	27,347	23.0	16,090	28.4	95	23.3	24.9
FY14E	129,701	9.2	29,292	22.6	17,304	7.5	102	21.7	21.6
FY15E	146,568	13.0	33,172	22.6	20,227	16.9	119	18.6	20.7

Figures in ₹ mn, # Includes Other Operating Income * Adjusted for Forex & Exceptional Items

Preparing for the next-big-thing: Biosimilars

The much discussed patent-cliff will phase out after FY14 and will be succeeded by a wave of generic opportunity in the Biosimilars space. DRL has already launched three products – Reditux, Cresp, and PeGrafeel – in 12 countries and is constantly working towards expanding its product offerings. The company is well positioned to benefit from the opening up of the biosimilar entry in the US.

Valuation

DRL leverages on its chemistry skills to identify and capitalize on niche opportunities with limited competition. The company has built significant API capabilities that support its fast growing generic formulations business. Notably, dependence on Betapharm has reduced significantly (14% of sales), and is unlikely to be a further drag on overall financials. At CMP, the stock trades at 21.7x FY14E & 18.6x FY15E earnings. We initiate coverage on Dr. Reddy's with 'Accumulate' recommendation and a target price of ₹ 2382 (20x to FY15E EPS).

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	96,737	116,266	130,401	147,268	Profit before tax	17,723	21,573	22,519	26,267
Other Operating Income/(Expense)	765	2,479	(700)	(700)	Depreciation & w.o.	5,213	5,546	6,195	6,784
Income from Operations	97,502	118,745	129,701	146,568	Net Interest Exp	529	(460)	578	121
Total Income	97,502	118,745	129,701	146,568	Direct taxes paid	(4,204)	(4,900)	(5,275)	(6,100)
Total Expenditure	72,997	91,398	100,409	113,396	Chg. in Working Capital	(4,909)	(5,686)	(3,809)	(3,730)
COGS	40,704	52,882	56,072	63,325	Impairment Charges	1,040	688	0	0
SGA	26,761	31,276	33,904	38,290	(A) CF from Opt. Activities	15,392	16,761	20,208	23,342
Other Expenses (R&D)	5,532	7,240	10,432	11,781	Capex	(7,959)	(6,232)	(7,280)	(7,800)
EBIDTA (excl. Other Income)	24,506	27,347	29,292	33,172	Free Cash Flow	7,433	10,529	12,928	15,542
Core EBITDA#	24,506	27,347	31,444	34,572	Inc./ (Dec.) in Investments	(10,795)	(227)	0	0
EBIDTA (incl. Other Income)	24,506	27,347	29,292	33,172	(B) CF from Inv. Activities	(18,754)	(6,459)	(7,280)	(7,800)
Interest Expense	690	0	578	121	Issue of Equity/ Preference	253	1	0	0
Interest Income	(161)	(460)	0	0	Inc./ (Dec.) in Debt	8,707	(2,563)	(7,279)	1,839
Net Interest Exp	529	(460)	578	121	Dividend Paid (Incl. Tax)	(2,331)	(2,378)	(2,463)	(2,548)
Gross Profit	23,977	27,807	28,714	33,051	Other (Bal.Fig)	(1,617)	269	882	1,339
Depreciation & Amortization	5,213	5,546	6,195	6,784	(C) CF from Fin. Activities	5,012	(4,671)	(8,860)	631
Profit Before Tax & EO Items	18,764	22,261	22,519	26,267	Net Change in Cash	1,650	5,631	4,068	16,172
Exceptional Items	1,040	688	0	0	Opening Cash balance	5,729	7,379	13,010	17,077
Profit Before Tax	17,723	21,573	22,519	26,267	Closing Cash balance	7,379	13,010	17,077	33,249
Tax	4,204	4,900	5,275	6,100	E-estimates				
Profit After Tax	13,519	16,673	17,244	20,167					
Forex Losses / (Gains)	(689)	0	0	0	IMPORTANT RATIOS				
Profit / (loss) from associates	54	104	60	60	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Profit	14,262	16,777	17,304	20,227	(A) Measures of Performance (%)				
Adj. PAT (Excl. Fx & EO)	12,533	16,090	17,304	20,227	Contribution Margin				
					EBIDTA Margin (incl. O.I.)	25.1	23.0	22.6	22.6
					Interest / Sales	0.7	0.0	0.4	0.1
					Gross Profit Margin	24.6	23.4	22.1	22.5
					Tax/PBT	23.7	22.7	23.4	23.2
					Net Profit Margin	14.6	14.1	13.3	13.8
					Core Net Profit Margin	14.6	14.1	14.3	14.8
					(B) Measures of Financial Status				
					Debt / Equity (x)	0.6	0.4	0.3	0.2
					Interest Coverage (x)	35.5	-	50.7	274.1
					Average Cost Of Debt (%)	2.5	0.0	2.1	0.4
					Debtors Period (days)	96	90	90	90
					Closing stock (days)	73	75	71	71
					Inventory Turnover Ratio (x)	5.0	4.9	5.1	5.1
					Fixed Assets Turnover (x)	2.6	3.0	3.3	3.6
					Working Capital Turnover (x)	3.1	2.8	2.6	2.1
					Non Cash Working Capital (₹ Mn)	23,526	29,212	33,021	36,751
					(C) Measures of Investment				
					Adj. EPS (₹) (excl EO)	86.0	102.8	101.9	119.1
					EPS (₹)	84.1	98.8	101.9	119.1
					CEPS (₹)	114.8	131.4	138.4	159.0
					DPS (₹)	13.7	14.0	14.5	15.0
					Dividend Payout (%)	16.3	14.2	14.2	12.6
					Profit Ploughback (%)	83.7	85.8	85.8	87.4
					Book Value (₹)	338.7	423.0	518.6	631.0
					RoANW (%)	24.2	24.9	21.6	20.7
					RoACE (%)	24.4	23.0	21.9	21.9
					RoAIC (%) (Excl Cash & Invest.)	26.6	25.7	25.5	27.7
					(D) Valuation Ratios				
					CMP (₹)	2,210	2,210	2,210	2,210
					P/E (x)	25.7	21.5	21.7	18.6
					P/Core EPS	26.3	22.4	21.7	18.6
					Market Cap. (₹ Mn)	374,816	375,346	375,346	375,346
					MCap/ Sales (x)	3.9	3.2	2.9	2.5
					EV (₹ Mn)	399,647	391,984	380,637	366,304
					EV/Sales (x)	4.1	3.4	2.9	2.5
					EV/EBDITA (x)	16.3	14.3	13.0	11.0
					P/BV (x)	6.5	5.2	4.3	3.5
					Dividend Yield (%)	0.6	0.6	0.7	0.7
					E-estimates				

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CMP: ₹ 2282

Target Price: ₹ 1900

Sell

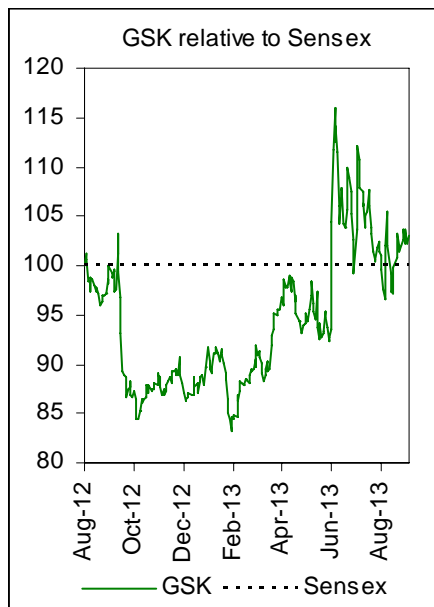
BSE Sensex	18234
NSE Nifty	5341

Scrip Details

Equity	₹ 847mn
Face Value	₹ 10/-
Market Cap	₹ 193bn
	USD 2885mn
52 week High / Low	₹ 2899 / 1931
Avg. Volume (no)	12245
BSE Code	500660
NSE Symbol	GLAXO
Bloomberg Code	GLXO IN
Reuters Code	GLAX.BO

Shareholding Pattern as on June'13(%)

Promoter	50.67
FIs	23.66
MF/Banks/FIs	10.59
Public / Others	15.08



GSK Pharma has access to its parent's product pipeline which is focussed on vaccines and oncology products. GSK has launched two patented products namely Revolade and Votrient from its parent GSK Plc's portfolio. However, sales have been impacted on account of supply constraints and inventory rationalisation. Moreover, the new DPCO 2013 is expected to have 5% impact on revenues in CY13E.

Investment Rationale

GSK India beneficiary of its parent's commitment

GSK Plc has firm commitments towards launching patented products in India through the listed entity. The Company's recent launches of the parent's shelf include Synflorix (paediatric pneumococcal vaccine), Votrient (pazopanib hydrochloride) for renal carcinoma and Revolade (eltrombopag) for platelet depletion. Its tiered pricing approach and significant domestic potential for these drugs facilitates gradual scalability.

DPCO 2013 impact - Major risk

The new DPCO 2013 policy poses a major risk for GSK. About 30% of the company's products are now under price control, compared to 25% earlier. Of its top five products, Augmentin, Calpol, Ceftum and Eltroxin together contribute ~ 20% of its domestic revenue. As per management, price control is expected to have an impact of 5% of revenues.

Cash balances unutilised

GSK has a cash/bank balance of ₹ 20.4bn i.e. ~₹ 241 per share. However, the lack of adequate opportunities to deploy these funds is a significant issue and given the current valuations, we are unlikely to see a share buy-back.

Valuations

GSK revenues have been impacted due to supply constraints and inventory rationalisation. In addition, the new DPCO 2013 is expected to have 5% impact on revenues in CY13E. Given the premium valuations (26.1x CY14E) and declining trend in margins, we recommend 'Sell' with a target price of ₹ 1900 (22x CY14E earnings).

Financials

Year	Net Sales#	% Growth	EBIDTA	OPM %	Adj.PAT*	% Growth	EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
CY11	23,759	10.8	7,824	32.9	6,314	8.6	74.5	8.6	30.6	32.8	40.7
CY12	26,303	10.7	8,191	31.1	6,772	7.3	79.9	7.3	28.5	34.5	42.3
CY13E	28,182	7.1	7,489	26.6	6,385	-5.7	75.4	-5.7	30.3	31.0	36.6
CY14E	31,593	12.1	8,711	27.6	7,311	14.5	86.3	14.5	26.4	33.5	40.1

Figures in ₹ mn, # Includes Operating Income, * Adjusted

INCOME STATEMENT					CASH FLOW				
Particulars	Dec11	Dec12	Dec13E	Dec14E	Particulars	Dec11	Dec12	Dec13E	Dec14E
Net Sales	23,380	25,999	27,882	31,283	Profit before tax	9,216	9,948	9,389	10,751
Operating Income	379	304	300	310	Depreciation & w.o.	204	178	250	310
Income From Operations	23,759	26,303	28,182	31,593	Net Interest Exp	0	0	0	0
Other income	1,596	1,935	2,150	2,350	Direct taxes paid	-2,902	-3,176	-3,005	-3,440
Total Income	25,355	28,238	30,332	33,943	Chg. in Working Capital	608	-454	245	309
Total Expenditure	15,935	18,112	20,693	22,882	Other	0	0	0	0
Operating Profit (excl. OI)	7,824	8,191	7,489	8,711	(A) CF from Opt. Activities	7,126	6,496	6,879	7,929
Operating Profit (incl. OI)	9,420	10,126	9,639	11,061	Capex	301	-400	-1,300	-650
Gross Profit	9,420	10,126	9,639	11,061	Free Cash Flow	7,427	6,096	5,579	7,279
Depreciation	204	178	250	310	(Inc)/ Dec. in Investments	5	572	-74	0
Profit Before Tax & EO Items	9,216	9,948	9,389	10,751	Others (Bal Fig)	-2,632	-1,217	0	0
Extra Ordinary Exps/(Income)	2,008	999	0	0	(B) CF from Invt. Activities	-2,326	-1,044	-1,374	-650
Profit Before Tax	7,208	8,949	9,389	10,751	Inc./(Dec.) in Debt	-3	-8	0	0
Tax	2,902	3,176	3,005	3,440	Dividend Paid (Incl. Tax)	-4,415	-4,905	-5,403	-5,893
Net Profit	4,306	5,773	6,385	7,311	(C) Cash Flow from Financing	-4,417	-4,913	-5,403	-5,894
BALANCE SHEET					Net Change in Cash	383	539	102	1,386
Particulars	Dec11	Dec12	Dec13E	Dec14E	Opening Cash balances	19,481	19,864	20,403	20,505
Sources of Funds					Closing Cash balances	19,864	20,403	20,505	21,891
Equity Capital	847	847	847	847	E-estimates				
Reserves (excl Rev Res)	18,352	19,253	20,235	21,652	IMPORTANT RATIOS				
Net Worth	19,199	20,100	21,082	22,499	Particulars	Dec11	Dec12	Dec13E	Dec14E
Unsecured Loans	49	41	41	41	(A) Measures of Performance (%)				
Loan Funds	49	41	41	41	Operating Profit Margin (excl. O.I.)	32.9	31.1	26.6	27.6
Deferred Tax Liability	-615	-865	-865	-865	Operating Profit Margin (incl. O.I.)	39.6	38.5	34.2	35.0
Total Capital Employed	18,634	19,276	20,258	21,675	Gross Profit Margin	39.6	38.5	34.2	35.0
Applications of Funds					Tax/PBT	40.3	35.5	32.0	32.0
Gross Block	2,717	3,221	4,171	5,171	Net Profit Margin	18.1	21.9	22.7	23.1
Less: Accumulated Depreciation	1,725	1,904	2,154	2,464	(B) Measures of Financial Status				
Net Block	991	1,317	2,017	2,707	Debtors Period (days)	13.3	16.3	14.0	13.0
Capital Work in Progress	254	150	500	150	Closing stock (days)	42.3	31.7	33.6	33.6
GOODWILL	0	0	0	0	Inventory Turnover Ratio (x)	7.1	9.2	8.7	8.7
Investments	1,598	1,026	1,100	1,100	Fixed Assets Turnover (x)	23.6	19.7	13.8	11.6
Current Assets, Loans & Advances					Working Capital Turnover (x)	1.5	1.5	1.7	1.8
Inventories	3,301	2,820	3,208	3,600	(C) Measures of Investment				
Sundry Debtors	853	1,159	1,069	1,114	EPS (₹) (excl EO)	74.5	79.9	75.4	86.3
Cash and Bank Balance	19,864	20,403	20,505	21,891	EPS (₹)	50.8	68.2	75.4	86.3
Loans and Advances	2,251	2,317	2,417	2,517	CEPS (₹)	53.2	70.3	78.3	90.0
Other Current Assets	690	839	881	925	DPS (₹)	45.0	50.0	55.0	60.0
<i>sub total</i>	26,959	27,538	28,081	30,047	Dividend Payout (%)	60.4	73.4	73.0	69.5
Less : Current Liabilities & Provisions					Profit Ploughback (%)	39.6	26.6	27.0	30.5
Current Liabilities	3,545	3,283	3,544	3,943	Book Value (₹)	226.7	237.3	248.9	265.6
Provisions	7,623	7,472	7,896	8,386	RoANW (%)	32.8	34.5	31.0	33.5
<i>sub total</i>	11,168	10,755	11,440	12,329	RoACE (%)	40.7	42.3	36.6	40.1
Net Current Assets	15,790	16,783	16,641	17,718	Return on Avg. Cap. Employed (%)	-297.8	-321.8	-413.7	-630.9
Total Assets	18,634	19,276	20,258	21,675	(D) Valuation Ratios				
E-estimates					Market Price - Average (₹)	2,282	2,282	2,282	2,282
					Price / Earnings Ratio - Average (x)	30.6	28.5	30.3	26.4
					Average Market Cap. (₹ Mn.)	193,318	193,318	193,318	193,318
					Market Capitalisation to Sales (x)	8.3	7.4	6.9	6.2
					Enterprise Value (₹ Mn.)	173,503	172,956	172,854	171,468
					EV/Sales (x)	7.4	6.7	6.2	5.5
					EV/EBDITA (x)	22.2	21.1	23.1	19.7
					Market Price to Book Value (x)	10.1	9.6	9.2	8.6
					Dividend Yield (%)	2.0	2.2	2.4	2.6
					E-estimates				

CMP: ₹ 514

Target Price: ₹ 561

Accumulate

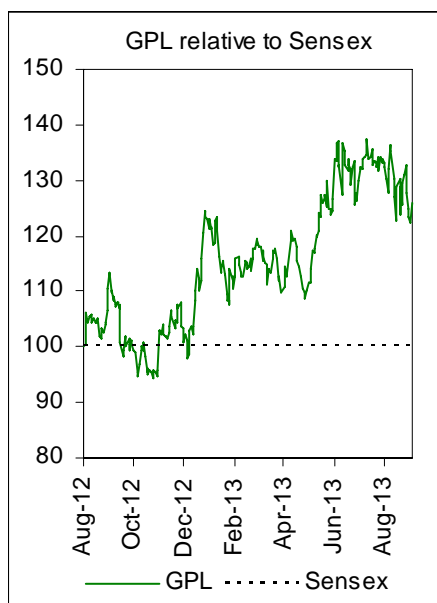
BSE Sensex	18235
NSE Nifty	5341

Scrip Details

Equity	₹ 271mn
Face Value	₹ 1/-
Market Cap	₹ 139bn
	USD 2079mn
52 week High / Low	₹ 612 / 386
Avg. Volume (no)	374912
BSE Code	532296
NSE Symbol	GLENMARK
Bloomberg Code	GNP IN
Reuters Code	GLEN.BO

Shareholding Pattern as on June'13(%)

Promoter	48.30
FII's	33.89
MF/Banks/FIs	7.08
Public / Others	10.73



All Round Growth....

Glenmark continues to build upon branded generics market across emerging markets including India and focus on specialty products such as oral contraceptives (OC) and dermatology in the US/Europe generics market. Moreover, Glenmark has a strong track record of monetizing molecules in early phase of R&D. We expect Glenmark to sustain revenue CAGR of 18% over FY13-15E.

Investment Rationale

US biz – focusing on specialty products for growth

We anticipate US generics segment (34% of sales) to be the key growth driver in the near future. The company is focusing on specialty therapies including dermatology and oral contraceptives which offer strong visibility in the long term. In the near term, growth would be supported by niche opportunities such as gVanos, gLocoid and 4-5 oral contraceptives. Moreover, Glenmark is focusing on oncology and controlled substances for future growth. Currently, the company has 53 ANDAs pending approval, of which 26 are Para IVs. We estimate US sales to register 18% CAGR over FY13-FY15E.

Domestic biz – Sustained momentum

Glenmark has recorded a robust 20% CAGR on its domestic formulation biz over FY08-13. As per ORG IMS Mat June 2013, Glenmark has gained three ranks to be 19th in the industry with dominant position in dermatology, respiratory and CVS segments. Going ahead, we believe the company would continue to outperform industry growth led by launch of inhalers in the Indian market and entry into women's healthcare. Moreover, the new pricing policy is expected to have negligible impact on domestic sales. Going ahead, we anticipate Glenmark to sustain 18% CAGR over FY13-15E in domestic sales.

R&D status – Focus back on out-licensing income

Glenmark is likely to report the NCE clinical data for various NCEs commencing with Asthma trial data for GRC 4039 (Revamilast) and three other NCEs by end of FY14E. Three molecules (GBR500, GRC15300 and mPGES-1 inhibitor) are currently out-licensed and may bring further milestone based payments in FY14E. However, our estimates exclude potential upsides from these.

Financials

Year	Net Sales	% Growth	EBIDTA	OPM %	Adj.PAT	% Growth	Adj.EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12	40,206	36.3	8,642	21.5	5,919	80.6	21.9	29.4	23.5	20.5	17.4
FY13	50,123	24.7	10,207	20.4	6,147	3.8	22.7	3.7	22.7	23.6	18.6
FY14E	58,548	16.8	12,146	20.7	7,201	17.1	26.6	17.1	19.3	23.1	20.0
FY15E	68,840	17.6	14,579	21.2	8,944	24.2	33.0	24.2	15.6	23.1	22.2

Figures in ₹ mn

Valuation

We expect Glenmark to post revenue CAGR of 18% and PAT CAGR of 19.8% over FY13-15E on the back of: a) strong pipeline of 53 ANDA's pending approval in US b) 18% CAGR in domestic formulation biz and 20% CAGR in semi-regulated markets and c) higher contribution from FTF and high margin products. At CMP, the stock trades at 19.3x FY14E & 15.6x FY15E earnings. We initiate coverage on Glenmark with 'Accumulate' recommendation and a target price of ₹ 561 (17x to FY15E EPS).

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	40,206	50,123	58,548	68,840	Profit before tax	6,197	7,337	8,891	11,029
Other Operational income	10	14	0	0	Depreciation & w.o.	979	1,270	1,500	1,750
Income for Operations	40,216	50,137	58,548	68,840	Net Interest Exp	1,466	1,600	1,755	1,800
Total Expenditure	31,746	40,024	46,502	54,362	Direct taxes paid	(238)	(1,107)	(1,600)	(1,985)
EBIDTA (Excl. Other Income)	8,470	10,113	12,046	14,479	Chg. in Working Capital	(1,050)	(2,272)	(1,242)	(2,480)
Other Income	171	94	100	100	(A) CF from Operating Activities	7,354	6,828	9,304	10,114
EBIDTA (Incl. Other Income)	8,642	10,207	12,146	14,579	Capex	(3,103)	(4,705)	(4,235)	(5,500)
Interest	1,466	1,600	1,755	1,800	Free Cash Flow	4,251	2,123	5,069	4,614
Gross Profit	7,176	8,607	10,391	12,779	Inc./ (Dec.) in Investments	128	0	0	0
Depreciation	979	1,270	1,500	1,750	(B) CF from Invst. Activities	(2,975)	(4,705)	(4,235)	(5,500)
Profit Before Tax & EO Items	6,197	7,337	8,891	11,029	Inc./ (Dec.) in Debt	(1,117)	2,882	(2,881)	(3,000)
Extra Ordinary Exps/(Income)	1,317	0	0	0	Interest exp net	(1,466)	(1,600)	(1,755)	(1,800)
Profit Before Tax	4,880	7,337	8,891	11,029	Dividend Paid (Incl. Tax)	(554)	(555)	(555)	(555)
Tax	238	1,107	1,600	1,985	Other (bal fig.)	0	0	(90)	(100)
Net Profit	4,643	6,230	7,291	9,044	(C) Cash Flow from Financing	(3,137)	728	(5,281)	(5,455)
Minority Interest	40	83	90	100	Net Change in Cash	1,242	2,851	(212)	(841)
Net Profit	4,603	6,147	7,201	8,944	Opening Cash balances	1,958	3,201	6,052	5,840
Adj.Net Profit	5,919	6,147	7,201	8,944	Closing Cash balances	3,201	6,052	5,840	4,999
BALANCE SHEET					IMPORTANT RATIOS				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Sources of Funds					(A) Measures of Performance (%)				
Equity Capital	271	271	271	271	Contribution Margin				
Other Reserves	23,746	27,359	34,006	42,395	EBIDTA Margin (excl. O.I.)	21.1	20.2	20.6	21.0
Net Worth	24,016	27,630	34,277	42,666	EBIDTA Margin (incl. O.I.)	21.1	20.2	20.6	21.0
Minority Interest	250	244	244	244	Gross Profit Margin	17.4	17.0	17.6	18.4
Secured Loans	6,875	3,678	5,000	5,000	Tax/PBT	4.9	15.1	18.0	18.0
Unsecured Loans	13,125	19,203	15,000	12,000	Net Profit Margin	11.4	12.3	12.3	13.0
Loan Funds	19,999	22,881	20,000	17,000					
Deferred Tax Liability	(2,674)	(3,803)	(3,803)	(3,803)	(B) As Percentage of Net Sales				
Total Capital Employed	41,592	46,952	50,718	56,107	Excise Duty % of Gross Sales	1.6	1.3	1.3	1.3
					Raw Material	33.5	33.0	30.2	29.7
Applications of Funds					Employee Expenses	15.6	15.7	15.9	15.9
Gross Block	26,334	28,834	31,334	33,834	Other Expenses	29.9	31.1	33.3	33.3
Less: Accumulated Depreciation	4,147	5,417	6,917	8,667					
Net Block	22,187	23,417	24,417	25,167	(C) Measures of Financial Status				
Capital Work in Progress	2,060	4,265	6,000	9,000	Debt / Equity (x)	0.8	0.8	0.6	0.4
Investments	181	181	181	181	Interest Coverage (x)	0.2	0.2	0.1	0.1
Current Assets, Loans & Advances					Average Cost Of Debt (%)	7.1	7.5	8.2	9.7
Inventories	7,877	8,435	8,720	10,083	Debtors Period (days)	113	119	105	105
Sundry Debtors	12,436	16,400	16,843	19,803	Closing stock (days)	72	61	54	53
Cash and Bank Balance	3,201	6,052	5,840	4,999	Inventory Turnover Ratio (x)	5.1	5.9	6.7	6.8
Loans and Advances	6,109	6,784	7,802	8,972	Fixed Assets Turnover (x)	1.5	1.7	1.9	2.0
Other Current Assets	609	603	603	603	Working Capital Turnover (x)	1.3	1.3	1.5	1.5
<i>sub total</i>	30,231	38,276	39,808	44,461	Non Cash Working Capital (₹ Mn)	27,030	32,224	33,968	39,462
Less : Current Liabilities & Provisions									
Current Liabilities	12,560	18,176	17,689	19,703	(D) Measures of Investment				
Provisions	509	1,011	2,000	3,000	EPS (₹) (excl EO)	21.9	22.7	26.6	33.0
<i>sub total</i>	13,068	19,187	19,689	22,703	EPS (₹)	21.9	22.7	26.6	33.0
Net Current Assets	17,163	19,089	20,119	21,758	CEPS (₹)	20.6	27.4	32.1	39.5
Total Assets	41,592	46,952	50,718	56,107	DPS (₹)	1.8	1.8	1.8	1.8
E-estimates					Dividend Payout (%)	8.2	7.9	6.8	5.5
					Profit Ploughback (%)	91.8	92.1	93.2	94.5
					Book Value (₹)	89.7	102.9	127.5	158.4
					RoANW (%)	20.5	23.6	23.1	23.1
					RoACE (%)	17.4	18.6	20.0	22.2
					RoAIC (%) (Excl Cash & Invest.)	23.4	26.5	29.0	31.3
					(E) Valuation Ratios				
					CMP (₹)	514	514	514	514
					P/E (x)	23.5	22.7	19.3	15.6
					Market Cap. (₹ Mn.)	139,107	139,271	139,271	139,271
					MCap/ Sales (x)	3.5	2.8	2.4	2.0
					EV (₹ Mn.)	155,905	156,100	151,431	146,272
					EV/Sales (x)	3.9	3.1	2.6	2.1
					EV/EBDITA (x)	18.4	15.4	12.6	10.1
					P/BV (x)	5.7	5.0	4.0	3.2
					Dividend Yield (%)	0.4	0.4	0.4	0.4
					E-estimates				

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CMP: ₹ 647

Target Price: ₹ 743

Accumulate

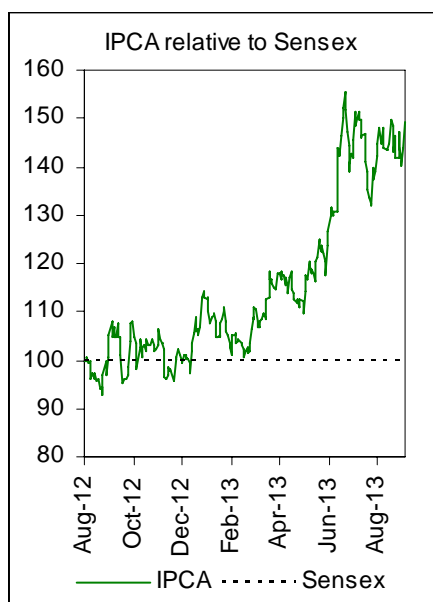
BSE Sensex	18235
NSE Nifty	5341

Scrip Details

Equity	₹ 252mn
Face Value	₹ 2/-
Market Cap	₹ 82bn
	USD 1217mn
52 week High / Low	₹ 708 / 389
Avg. Volume (no)	168437
BSE Code	524494
NSE Symbol	IPCALAB
Bloomberg Code	IPCA IN
Reuters Code	IPCA.BO

Shareholding Pattern as on June'13(%)

Promoter	45.89
FII's	22.96
MF/Banks/FIs	13.50
Public / Others	17.65



Entering the Big League...

IPCA has transformed itself from a leading API manufacturer to a fully integrated formulation company. The company has a dominant position in the anti-malaria segment in India with 48% market share in FY13. The domestic formulations segment is expected to record 15% CAGR over FY13-15E, led by increasing contribution from CVS and pain segment. Moreover, new pricing policy will not have any material impact on domestic sales. We anticipate export formulations to register 24% growth over FY13-15E mainly driven by increasing contribution from institutional based sales and ramp up in its US generics biz. In addition, commercialization of Indore SEZ shall do away with capacity constraints and pave way for market share gains in existing products and facilitate new launches.

Investment Rationale

Integrated Generic Play - IPCA has transformed itself from an API manufacturer to a fully integrated formulation company. Formulations constitute 76% of the product mix with APIs mainly for captive consumption. The company follows a two pronged growth strategy viz., emphasis on branded formulations with front end presence in fast growing emerging markets and is a preferred supplier for generics (APIs/formulations) to its partners based in the regulated markets and thus stays away from any patent litigation.

Domestic business- No material impact of new pricing policy: IPCA holds 1.7% market share in the domestic pharma market (MAT June'13). Anti-malarials, CVS and pain management constitute more than 50% of the domestic business. As per company, the new DPCO 2013 coverage is expected to increase to ₹1.7bn from ₹ 710mn (under DPCO 1995). However, the impact could be partially set off by 10% price hike in the portfolio coming out of DPCO 2013, 7.5% price hike taken in portfolios common to DPCO 1995 and 2013 and existing products outside price control. We anticipate the company to witness a growth of 14% in FY14E and 16% in FY15E.

US business- growth to be driven by Indore SEZ commercialization: IpcA faces capacity constraints and has not been able to launch new products/increase market share in existing products. We anticipate Indore

Financials

Year	Net Sales#	% Growth	EBIDTA	OPM %	Adj.PAT	% Growth	EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12	23,587	24.2	5,135	21.8	3,298	50.3	26.1	49.8	24.7	28.6	25.4
FY13	28,131	19.3	6,232	22.2	3,867	17.3	30.6	17.2	21.1	27.3	26.1
FY14E	32,711	16.3	7,274	22.2	4,582	18.5	36.3	18.5	17.8	26.0	26.2
FY15E	38,322	17.2	8,681	22.7	5,515	20.4	43.7	20.4	14.8	25.3	26.7

Figures in ₹ mn, # Includes other operating income .

SEZ to be commercialized in Q4FY14 and growth to revive from FY15E onwards. Over next 2-3 years, incremental revenue of USD 80mn is expected from Indore SEZ as per management. We estimate US business to grow by 51% CAGR over FY13-15E to ₹4.2bn, led by incremental revenues due to Indore SEZ commercialization (USD 10mn in FY14E and USD 30mn in FY15E).

Institutional business to sustain growth: Currently, ~95% of institutional business is primarily focused on malaria and sold in African countries where the incidence of malaria is very high. The company has guided for 17% revenue growth in FY14E, on the back of strong order book position and is expected to pick-up in H2FY14E. Notably, funding commitment over AMFm (Affordable Medicines Facility- Malaria) programs and increased off take of Artemether-Lumefantrine (AL) formulation ensures revenue visibility in its institutional business. The management believes the institutional business can grow to ₹ 8bn from guided sales of ₹ 4.6bn in FY14 over the next three years.

Valuation

We expect acceleration in export formulation revenues mainly led by a) uptick in US revenues-commercialization of Indore SEZ in Q4FY14E, b) sustained growth in its institutional business and c) gradual recovery in domestic formulations hereon shall add to growth momentum. We estimate adjusted earnings to record 22% CAGR over FY13-15E. At CMP, the stock trades at 17.8x FY14E and 14.8x FY15E earnings. We recommend '**Accumulate**' on the stock with a target price of ₹ 743 (17x FY15E EPS).

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	23,140	27,537	32,161	37,822	Profit before tax	4,170	5,174	6,032	7,258
Operating Income	448	595	550	500	Depreciation & w.o.	671	867	1,027	1,172
Income from Operations	23,587	28,131	32,711	38,322	Net Interest Exp	413	334	415	402
Other income	120	143	200	150	Direct taxes paid	(881)	(1,299)	(1,450)	(1,743)
Total Income	23,707	28,274	32,911	38,472	Chg. in Working Capital	(435)	(1,635)	(1,764)	(2,841)
Total Expenditure	18,452	21,899	25,437	29,641	(A) CF from Opt. Activities	3,938	3,441	4,260	4,248
Other Expenses	5,966	7,015	7,952	9,233	Capex	(3,289)	(3,292)	(2,800)	(2,800)
EBIDTA (Excl. Other Income)	5,135	6,232	7,274	8,681	Free Cash Flow	649	149	1,460	1,448
EBIDTA (Incl. Other Income)	5,255	6,375	7,474	8,831	(B) CF from Invst. Activities	(3,289)	(3,292)	(2,800)	(2,800)
Interest	413	334	415	402	Issue of Equity/ Preference	13	0	0	0
Gross Profit	4,842	6,041	7,059	8,430	Inc./(Dec.) in Debt	703	87	(90)	(100)
Depreciation	671	867	1,027	1,172	Interest exp net	(413)	(334)	(415)	(402)
Profit Before Tax & EO Items	4,170	5,174	6,032	7,258	Dividend Paid (Incl. Tax)	(468)	(660)	(807)	(953)
Extra Ordinary Exps/(Income)	0	0	0	0	Other (Bal.fig)	(466)	(0)	(0)	(0)
Profit Before Tax	4,170	5,174	6,032	7,258	(C) Cash Flow from Financing	(631)	(907)	(1,312)	(1,455)
Tax	881	1,299	1,450	1,743	Net Change in Cash	18	(758)	148	(7)
Net Profit	3,289	3,875	4,582	5,515	Opening Cash balances	104	122	(644)	(496)
Share of associates	(9)	8	0	0	Closing Cash balances	122	(644)	(496)	(503)
Adj.Net Profit	3,298	3,867	4,582	5,515	E-estimates				
Forex Losses/(Gains)	527	631	0	0					
PAT	2,771	3,236	4,582	5,515					

BALANCE SHEET					IMPORTANT RATIOS				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Sources of Funds					(A) Measures of Performance (%)				
Equity Capital	252	252	252	252	Contribution Margin				
Share Premium	436	436	436	436	EBIDTA Margin (excl. O.I.)	21.8	22.2	22.2	22.7
Other Reserves	11,852	15,059	18,834	23,396	EBIDTA Margin (incl. O.I.)	22.3	22.7	22.8	23.0
Net Worth	12,540	15,747	19,522	24,084	Interest / Sales	1.8	1.2	1.3	1.1
Secured Loans	5,038	5,063	4,963	4,813	Gross Profit Margin	20.4	21.4	21.4	21.9
Unsecured Loans	984	1,045	1,055	1,105	Tax/PBT	21.1	25.1	24.0	24.0
Loan Funds	6,022	6,108	6,018	5,918	Net Profit Margin	14.0	13.7	14.0	14.4
Deferred Tax Liability	932	932	932	932					
Total Capital Employed	19,493	22,787	26,472	30,934	(B) As Percentage of Net Sales				
					Raw Material	38.7	39.0	39.5	39.7
Applications of Funds					Employee Expenses	14.2	13.9	13.9	13.5
Gross Block	13,150	16,305	19,596	22,396	Other Expenses	25.3	24.9	24.3	24.1
Less: Accumulated Depreciation	3,945	4,812	5,839	7,010					
Net Block	9,205	11,493	13,758	15,386	(C) Measures of Financial Status				
Capital Work in Progress	1,155	1,292	800	800	Debt / Equity (x)	0.5	0.4	0.3	0.2
Goodwill	236	236	236	236	Interest Coverage (x)	12.7	19.1	18.0	22.0
Investments	341	341	341	341	Average Cost Of Debt (%)	7.3	5.5	6.8	6.7
Current Assets, Loans & Advances					Debtors Period (days)	55	70	71	73
Inventories	6,699	7,016	8,283	10,051	Closing stock (days)	106	93	94	97
Sundry Debtors	3,491	5,281	6,256	7,564	Inventory Turnover Ratio (x)	3.5	3.9	3.9	3.8
Cash and Bank Balance	122	(644)	(496)	(503)	Fixed Assets Turnover (x)	1.8	1.7	1.6	1.7
Loans and Advances	2,025	2,125	2,225	2,425	Working Capital Turnover (x)	2.7	2.9	2.8	2.7
Other Current Assets					Non Cash Working Capital (₹ Mn)	8,435	10,070	11,834	14,674
<i>sub total</i>	12,337	13,779	16,268	19,538					
Less : Current Liabilities & Provisions					(D) Measures of Investment				
Current Liabilities	3,403	3,852	4,391	4,680	EPS (₹) (excl EO)	26.1	30.6	36.3	43.7
Provisions	377	500	540	686	EPS (₹)	22.0	25.6	36.3	43.7
<i>sub total</i>	3,780	4,353	4,930	5,367	CEPS (₹)	31.5	37.5	44.4	53.0
Net Current Assets	8,556	9,426	11,338	14,171	DPS (₹)	3.2	4.5	5.5	6.5
					Dividend Payout (%)	14.5	17.6	15.1	14.9
Total Assets	19,493	22,787	26,472	30,934	Profit Ploughback (%)	85.5	82.4	84.9	85.1
E-estimates					Book Value (₹)	99.4	124.8	154.7	190.8
					RoANW (%)	28.6	27.3	26.0	25.3
					RoACE (%)	25.4	26.1	26.2	26.7
					RoAIC (%) (Excl Cash & Invest.)	25.5	25.7	25.6	26.2
					(E) Valuation Ratios				
					CMP (₹)	647	647	647	647
					P/E (x)	24.7	21.1	17.8	14.8
					Market Cap. (₹ Mn.)	81,569	81,601	81,601	81,601
					MCap/ Sales (x)	3.5	3.0	2.5	2.2
					EV (₹ Mn.)	87,468	88,353	88,115	88,022
					EV/Sales (x)	3.8	3.2	2.7	2.3
					EV/EBDITA (x)	17.0	14.2	12.1	10.1
					P/BV (x)	6.5	5.2	4.2	3.4
					Dividend Yield (%)	0.5	0.7	0.9	1.0
					E-estimates				

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CMP: ₹ 840

Target Price: ₹ 965

Accumulate

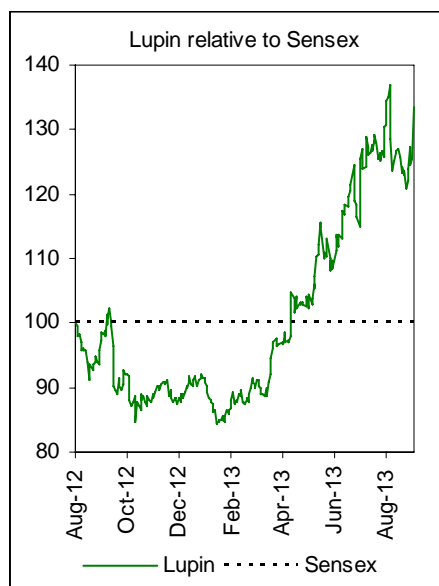
BSE Sensex	18235
NSE Nifty	5341

Scrip Details

Equity	₹ 895mn
Face Value	₹ 2/-
Market Cap	₹ 376bn
	USD 5613mn
52 week High / Low	₹ 908 / 540
Avg. Volume (no)	1274208
BSE Code	500257
NSE Symbol	LUPIN
Bloomberg Code	LPC IN
Reuters Code	LUPN.BO

Shareholding Pattern as on June'13(%)

Promoter	46.81
FII's	30.67
MF/Banks/FIs	12.40
Public / Others	10.12



Fundamentally Healthy...

Lupin is our preferred pick on account of successful transformation from a Tier-II API manufacturer to a fully integrated global generic player. It has managed to deliver superior growth of 44% CAGR in export formulations; 20% CAGR in domestic formulations over FY08-13 aided by selective launches in niche fast-growing therapeutic areas. We expect the export formulation business to grow by 14% CAGR over FY13-15E led by monetization of its generic pipeline (FTF's and OC's) in the US market and consolidation of its position in the Japanese market. Growth in domestic formulations (16% CAGR over FY13-15E) business will be primarily driven by new launches and incremental sales from Eli Lilly alliance.

Investment Rationale

US generics – targeting niche opportunities

Lupin has differentiated itself from other Indian generic companies in the US by a) focusing on branded innovator products b) launching low-competition/patent challenge product in the US and c) in-licensing products. The company is focusing on complex molecules and therapies including OC's, dermatology and ophthalmology. The company has 65 ANDAs pending approval, of which 38 are Para IVs and 8 FTF opportunities. We anticipate limited competition generic launches in US (Niaspan, Renagel, Trizivir, Lunesta, Zymar, TriLipix and Asacol) to aid growth trajectory. In addition, launch of Seasonique and Yasmin in July'13, to further ramp-up sales in US going ahead. We estimate US sales to register USD 740mn in FY14E and USD 850mn in FY15E.

Japan biz – Increasing profitability

Lupin has built up a sizeable presence in the Japan market through the acquisition of Kyowa and I'rom. The company aims to increase its profitability with captive API sourcing. We estimate Japan biz to record 16% CAGR over FY13-15E to USD 275mn.

Domestic Formulation business – Shifting focus from acute to chronic

Lupin expects its strategy to focus on chronic therapies (60% contribution to domestic business; aims to increase it to 70% in next couple of years) to help it grow faster than industry growth of 12%. While CVS, metabolic,

Financials

Year	Net Sales#	% Growth	EBIDTA	OPM %	Adj.PAT*	% Growth	EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12	70,829	21.7	14,447	20.4	8,875	0.9	19.8	0.9	41.1	24.3	23.4
FY13	96,413	36.1	22,700	23.5	13,404	51.0	30.0	51.0	27.2	29.3	30.7
FY14E	111,299	15.4	26,155	23.5	15,572	16.2	34.8	16.2	23.4	26.8	30.7
FY15E	128,689	15.6	30,885	24.0	17,990	15.5	40.2	15.5	20.3	24.9	31.1

Figures in ₹ mn, * Adjusted, # Includes income from Operations

ophthalmology, respiratory and gastro would remain, women healthcare and IV fluids would provide growth opportunities. We expect Lupin's domestic formulations to post revenue of 16% CAGR over FY13-15E, led by a rapidly expanding presence in fast growing chronic therapeutic areas like CVS and anti-diabetes, increase in its field force and new launches. We believe Lupin will continue its out-performance of the industry as historically it has grown much faster than the industry, clocking revenue CAGR of 20% over FY08-13.

Valuations

We expect Lupin to register earnings CAGR of 14% over FY13-15E, led by limited competition generic launches in US (Niaspan, Renagel, Trizivir, Lunesta, Zymar, TriLipix and Asacol). Its business model enables healthy cash flow generation and augments requisite growth funding. The company continues to seek high-potential, low-risk acquisitions in key markets which shall further complement its organic growth momentum. At CMP, the stock trades at 24.2x FY14E and 20.9x FY15E earnings. We recommend 'Accumulate' on the stock with a target price of ₹ 965 (24x FY15E earnings). We continue to have Lupin in our preferred picks list.

INCOME STATEMENT					CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E	Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	69,597	94,616	109,299	126,589	Profit before tax	11,961	19,246	22,211	26,128
Operating income	1,232	1,797	2,000	2,100	Depreciation & w.o.	2,275	3,322	4,318	5,182
Income from Operations	70,829	96,413	111,299	128,689	Net Interest Exp	355	410	526	575
Other Income	144	279	900	1,000	Direct taxes paid	(3,086)	(5,842)	(6,663)	(7,838)
Total Income	70,973	96,692	112,199	129,689	Chg in Working Capital	(5,931)	(5,896)	(6,607)	(6,911)
Total Expenditure	56,382	73,713	85,144	97,804	(A) CF from Opt. Activities	5,574	11,241	13,785	17,136
Other Expenses	20,648	25,745	30,051	34,746	Capex	(10,144)	(5,500)	(6,000)	(6,000)
EBIDTA (Excl. Other Income)	14,447	22,700	26,155	30,885	Free Cash Flow	(4,570)	5,741	7,785	11,136
EBIDTA (Incl. Other Income)	14,591	22,978	27,055	31,885	Inc./ (Dec.) in Investments	4	0	0	0
Interest	355	410	526	575	Other (Bal.Fig)	1,346	(29)	102	(278)
Gross Profit	14,236	22,568	26,529	31,310	(B) CF from Invnt. Activities	(8,794)	(5,529)	(5,898)	(6,278)
Depreciation	2,275	3,322	4,318	5,182	Issue of Equity/ Preference	52	2	0	0
Profit Before Tax & EO Items	11,961	19,246	22,211	26,128	Inc./ (Dec.) in Debt	4,776	(956)	(3,944)	(1,000)
Profit Before Tax	11,961	19,246	22,211	26,128	Interest exp net	(355)	(410)	(526)	(575)
Tax	3,086	5,842	6,663	7,838	Dividend Paid (Incl. Tax)	(1,430)	(1,790)	(2,238)	(2,685)
Net Profit before Minority Interest	8,875	13,404	15,547	18,290	(C) CF from Financing	3,044	(3,155)	(6,708)	(4,260)
Share of Associates	0	0	(300)	0	Net Change in Cash	(176)	2,557	1,179	6,597
Minority Interest	0	0	275	300	Opening Cash balances	4,201	4,025	6,582	7,761
Net Profit	8,875	13,404	15,572	17,990	Closing Cash balances	4,025	6,582	7,761	14,358
BALANCE SHEET					E-estimates				
Particulars	Mar12	Mar13	Mar14E	Mar15E	IMPORTANT RATIOS				
Sources of Funds					Particulars	Mar12	Mar13	Mar14E	Mar15E
Equity Capital	894	895	895	895	(A) Measures of Performance (%)				
Share Premium	5,249	5,249	5,249	5,249	Contribution Margin				
Other Reserves	33,987	45,282	58,494	73,620	EBIDTA Margin (excl. O.I.)	20.4	23.5	23.5	24.0
Net Worth	40,129	51,426	64,637	79,764	EBIDTA Margin (incl. O.I.)	20.6	23.8	24.3	24.8
Secured Loans	8,170	10,979	8,000	7,500	Interest / Sales	0.5	0.4	0.5	0.5
Unsecured Loans	8,230	4,465	3,500	3,000	Gross Profit Margin	20.1	23.4	23.8	24.3
Loan Funds	16,400	15,444	11,500	10,500	Tax/PBT	25.8	30.4	30.0	30.0
Deferred Tax Liability	1,442	1,532	1,532	1,532	Net Profit Margin	12.5	13.9	14.0	14.0
Minority Interest	723	923	1,123	1,323	(B) As Percentage of Net Sales				
Total Capital Employed	58,695	69,325	78,792	93,119	Raw Material	36.8	36.8	36.0	35.5
Applications of Funds					Employee Expenses	13.7	13.0	13.5	13.5
Gross Block	36,878	44,852	50,852	56,852	Other Expenses	29.2	26.7	27.0	27.0
Less: Accumulated Depreciation	14,422	17,744	22,062	27,244	(C) Measures of Financial Status				
Net Block	22,457	27,108	28,790	29,608	Debt / Equity (x)	0.4	0.3	0.2	0.1
Capital Work in Progress	4,974	2,500	2,500	2,500	Interest Coverage (x)	41.1	56.0	51.4	55.5
Goodwill on consolidation	5,040	5,040	5,040	5,040	Average Cost Of Debt (%)	2.5	2.6	3.9	5.2
Investments	28	28	28	28	Debtors Period (days)	91	85	88	88
Current Assets, Loans & Advances					Closing stock (days)	91	87	84	84
Inventories	17,327	22,552	25,154	29,133	Inventory Turnover Ratio (x)	4.0	4.2	4.3	4.3
Sundry Debtors	17,318	22,034	26,352	30,520	Fixed Assets Turnover (x)	1.9	2.1	2.1	2.2
Cash and Bank Balance	4,025	6,582	7,761	14,358	Working Capital Turnover (x)	2.7	2.7	2.6	2.3
Loans and Advances	7,705	8,841	9,807	10,944	Non Cash Working Capital (₹ Mn)	22,171	28,067	34,674	41,585
<i>sub total</i>	<i>46,374</i>	<i>60,010</i>	<i>69,073</i>	<i>84,955</i>	(D) Measures of Investment				
Less : Current Liabilities & Provisions					EPS (₹) (excl EO)	19.8	30.0	34.8	40.2
Current Liabilities	16,891	21,817	22,567	24,414	EPS (₹)	19.8	30.0	34.8	40.2
Provisions	3,287	3,544	4,071	4,598	CEPS (₹)	25.0	37.4	44.4	51.8
<i>sub total</i>	<i>20,178</i>	<i>25,361</i>	<i>26,638</i>	<i>29,012</i>	DPS (₹)	3.2	4.0	5.0	6.0
Net Current Assets	26,196	34,649	42,434	55,943	Dividend Payout (%)	16.1	13.4	14.4	14.9
Total Assets	58,695	69,325	78,792	93,119	Profit Ploughback (%)	83.9	86.6	85.6	85.1
E-estimates					Book Value (₹)	89.8	114.9	144.4	178.2
					RoANW (%)	24.3	29.3	26.8	24.9
					RoACE (%)	23.4	30.7	30.7	31.1
					RoAIC (%) (Excl Cash & Invest.)	25.4	33.5	34.0	35.7
					(E) Valuation Ratios				
					CMP (₹)	840	840	840	840
					P/E (x)	42.4	28.1	24.2	20.9
					Market Cap. (₹ Mn.)	375,468	376,099	376,099	376,099
					MCap/ Sales (x)	5.4	4.0	3.4	3.0
					EV (₹ Mn.)	387,844	384,961	379,838	372,240
					EV/Sales (x)	5.6	4.1	3.5	2.9
					EV/EBDITA (x)	26.8	17.0	14.5	12.1
					P/BV (x)	9.4	7.3	5.8	4.7
					Dividend Yield (%)	0.4	0.5	0.6	0.7
					E-estimates				

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CMP: ₹ 510

Target Price: ₹ 603

Accumulate

BSE Sensex	18235
NSE Nifty	5341

Scrip Details

Equity	₹ 1036mn
Face Value	₹ 1/-
Market Cap	₹ 1057bn
	USD 16bn
52 week High / Low	₹ 581 / 321
Avg. Volume (no)	1,562,022
BSE Code	524715
NSE Symbol	SUNPHARMA
Bloomberg Code	SUNP IN
Reuters Code	SUN.BO

Shareholding Pattern as on June'13(%)

Promoter	63.68
FII's	22.76
MF/Banks/FIs	3.24
Public / Others	10.32

Firing on all cylinders

Sun Pharma (SUNP) has outperformed market growth over the past seven years (CAGR of 17.5% over FY03-13) and has consistently improved its market share. In addition, Sun has strengthened its presence in the US market by acquisition of URL Pharma (adds 107 products to US portfolio), DUSA pharma (gives access to branded dermatology product portfolio) and Taro (dermatology and topical products). We estimate Sun to report revenue CAGR of 19.5% over FY13-15E and earnings CAGR of 18.5% over FY13-15E.

Investment Rationale

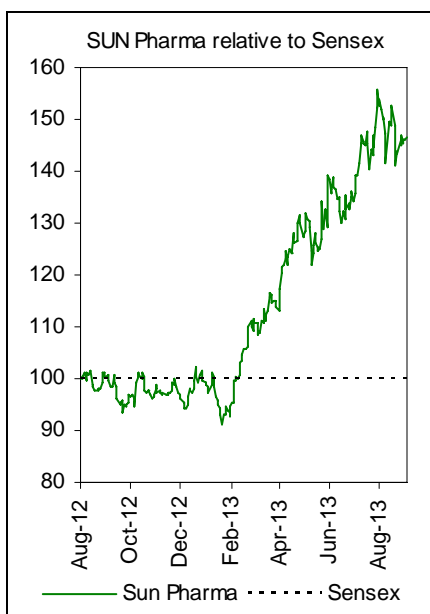
Domestic Formulations – Growth led by chronic therapies

SUNP has recorded a robust 17.5% CAGR on its domestic formulation biz over FY06-13. As per AIOCD-AWACS June 2013, SUNP is ranked 2nd and holds 5.1% market share in the Indian pharma market. The company has dominant position in CVS, CNS and gastro portfolio. Going ahead, we believe the company would continue to outperform industry growth led by new product launches and market share gain in existing product portfolio. Moreover, the new pricing policy is expected to have negligible impact on domestic sales. We anticipate SUNP to sustain 18% CAGR over FY13-15E in domestic sales.

US generics – Niche filings

We anticipate US generics segment excl. Taro (30% of sales) to be the key growth driver in the near future. The company is focusing on complex molecules and therapies including controlled substances, dermatology and injectables which offer strong visibility in the long term. In July 2013, SUNP launched gPrandin with 180 day exclusivity in US. Prandin has market size of USD200mn. SUNP expects entry of atleast 3 generic players post conclusion of 180 day exclusivity.

- **Taro Pharma:** Management has reiterated that the price increase undertaken by Taro for some of its dermatology products may not be sustainable in the long-term. It also indicated that competition for its top product, Nystatin, has increased with Sandoz re-entering the market. The company expects increased R&D investments to strengthen Taro's generic pipeline.



Financials

Year	Net Sales#	% Growth	EBIDTA	OPM %	Adj.PAT	% Growth	EPS (₹)	% Growth	PER (x)	ROANW(%)	ROACE (%)
FY12	80,197	40.2%	32,648	40.7	22,653	24.7	21.9	24.7	23.3	22.8	29.7
FY13	112,999	40.9%	49,673	44.0	35,916	58.6	34.7	58.6	14.7	29.7	35.6
FY14E	133,182	17.9%	58,295	43.8	44,696	24.4	21.6	-37.8	23.7	33.1	35.7
FY15E	160,838	20.8%	68,512	42.6	49,977	11.8	24.1	11.8	21.2	31.3	35.7

Figures in ₹ mn, #Includes Other Operating Income

- **URL Pharma and Dusa Acquisition:** SUNP indicated that the performance of URL Pharma/DUSA Pharma has been above expectations so far. While the company has not disclosed the revenue size of URL Pharma, it had earlier indicated that the profit margins are well below the consolidated entity. We expect US biz to grow at 15% CAGR over FY13-15E.

Valuation

We expect SUNP to post revenue CAGR of 19.5% and PAT CAGR of 18.5% over FY13-15E on the back of: 1) Superior revenue mix; 2) Domestic market growth rate to be higher than the market @ 18%; 3) Higher R&D expenditure productivity 4) Competition in Taro products leading to price normalization; 5) Increased visibility in US on account of upsides from URL and DUSA acquisitions. At CMP, the stock trades at 23.7x FY14E & 21.2x FY15E earnings. We initiate coverage on SUNP with 'Accumulate' recommendation and a target price of ₹ 603 (25x FY15E EPS).

INCOME STATEMENT				
Particulars	Mar12	Mar13	Mar14E	Mar15E
Net Sales	80,057	112,389	132,832	160,488
Other Operational income	141	610	350	350
Income from Operations	80,197	112,999	133,182	160,838
Total Expenditure	47,550	63,326	74,887	92,326
EBIDTA (Excl. Other Income)	32,648	49,673	58,295	68,512
Other Income	4,100	3,117	3,400	4,800
EBIDTA (Incl. Other Income)	36,747	52,790	61,695	73,312
Interest	282	443	450	451
Gross Profit	36,465	52,346	61,245	72,861
Depreciation	2,912	3,362	4,982	4,737
Profit Before Tax & EO Items	33,554	48,985	56,264	68,124
Extra Ordinary Exps/(Income)	0	5,836	25,174	0
Profit Before Tax	33,554	43,149	31,090	68,124
Tax	3,132	8,206	6,218	12,262
Net Profit	30,422	34,943	24,872	55,861
Minority Interest	3,855	4,863	5,349	5,884
Net Profit	26,567	30,081	19,523	49,977
Adjusted Net Profit	22,653	35,916	44,696	49,977

BALANCE SHEET

Particulars	Mar12	Mar13	Mar14E	Mar15E
Sources of Funds				
Equity Capital	1,036	1,036	2,071	2,071
Other Reserves	110,410	129,082	137,943	177,258
Net Worth	111,445	130,118	140,014	179,330
Minority Interest	11,615	16,351	22,891	32,048
Secured Loans	1,554	1,153	1,153	1,153
Unsecured Loans	1,096	830	830	830
Loan Funds	2,650	1,982	1,982	1,982
Deferred Tax Liability	1,636	2,064	2,579	3,224
Total Capital Employed	127,346	150,514	167,467	216,583
Applications of Funds				
Gross Block	54,269	74,430	81,930	90,236
Less: Accumulated Depreciation	24,973	28,624	32,842	49,088
Net Block	29,295	45,806	49,088	41,148
Capital Work in Progress	3,447	4,965	6,455	8,391
Investments	22,129	24,116	25,000	25,000
Current Assets, Loans & Advances				
Inventories	20,870	25,778	30,329	36,638
Sundry Debtors	19,261	18,408	21,789	26,768
Cash and Bank Balance	33,672	40,587	45,849	93,888
Loans and Advances	16,877	21,660	25,836	31,211
<i>sub total</i>	90,680	106,433	123,804	188,505
Less : Current Liabilities & Provisions				
Current Liabilities	14,499	15,855	17,973	21,712
Provisions	10,541	24,126	28,083	33,925
<i>sub total</i>	25,040	39,981	46,056	55,636
Net Current Assets	65,640	66,451	77,748	132,869
Deferred Tax Asset	6,835	9,176	9,176	9,176
Total Assets	127,346	150,514	167,466	216,583

E-estimates

CASH FLOW				
Particulars	Mar12	Mar13	Mar14E	Mar15E
Profit before tax	29,699	38,286	25,741	62,240
Depreciation & w.o.	2,912	3,362	4,982	4,737
Direct taxes paid	(3,818)	(8,980)	(7,767)	(13,811)
Chg. in Working Capital	(9,844)	4,191	(5,519)	(6,437)
(A) CF from Opt. Activities	18,948	36,858	17,437	46,729
Capex	(9,887)	(21,680)	(8,990)	(10,242)
Free Cash Flow	9,061	15,179	8,448	36,487
Inc./ (Dec.) in Investments	169	(1,987)	(884)	0
(B) CF from Investing Activities	(9,719)	(23,667)	(9,874)	(10,242)
Issue of Equity/ Preference	0	0	1,036	0
Inc./ (Dec.) in Debt	(1,001)	(668)	0	0
Interest exp net	(282)	(443)	(450)	(451)
Dividend Paid (Incl. Tax)	(4,039)	(4,557)	(9,113)	(9,113)
(C) CF from Financing	(5,322)	(5,668)	(8,528)	(9,564)
Net Change in Cash	5,992	8,256	(1,278)	38,882
Opening Cash balances	22,046	33,672	40,587	45,849
Closing Cash balances	28,039	41,928	39,309	84,731

E-estimates

IMPORTANT RATIOS

Particulars	Mar12	Mar13	Mar14E	Mar15E
(A) Measures of Performance (%)				
Contribution Margin				
EBIDTA Margin (excl. O.I.)	40.7	44.0	43.8	42.6
EBIDTA Margin (incl. O.I.)	45.8	46.7	46.3	45.6
Interest / Sales	0.4	0.4	0.3	0.3
Gross Profit Margin	45.5	46.3	46.0	45.3
Tax/PBT	9.3	19.0	20.0	18.0
Net Profit Margin	33.1	26.6	14.7	31.1
(B) As Percentage of Net Sales				
Raw Material	20.5	18.4	23.2	25.8
Employee Expenses	14.8	13.6	12.9	12.0
R&D Expenses	5.5	6.2	5.0	4.9
Other Expenses	5.5	6.2	5.0	4.9
(C) Measures of Financial Status				
Interest Coverage (x)	130.3	119.1	137.1	162.6
Average Cost Of Debt (%)	9.0	19.1	22.7	22.8
Debtors Period (days)	88	60	60	61
Closing stock (days)	95	84	83	83
Inventory Turnover Ratio (x)	3.8	4.4	4.4	4.4
Fixed Assets Turnover (x)	1.5	1.5	1.6	1.8
Working Capital Turnover (x)	1.2	1.7	1.7	1.2
Non Cash Working Capital (₹ Mn)	31,969	25,864	31,899	38,981
(D) Measures of Investment				
EPS (₹) (excl EO)	21.9	34.7	21.6	24.1
EPS (₹)	25.7	29.0	9.4	24.1
CEPS (₹)	28.5	32.3	11.8	26.4
DPS (₹)	3.9	4.4	4.4	4.4
Dividend Payout (%)	15.2	15.1	46.7	18.2
Profit Ploughback (%)	84.8	84.9	53.3	81.8
Book Value (₹)	107.6	125.6	67.6	86.6
RoANW (%)	22.8	29.7	33.1	31.3
RoACE (%)	29.7	35.6	35.7	35.7
RoAIC (%) (Excl Cash & Invest.)	39.3	48.6	49.0	56.1
(E) Valuation Ratios				
CMP (₹)	510	510	510	510
P/E (x)	23.3	14.7	23.7	21.2
Market Cap. (₹ Mn.)	528,622	528,622	1,057,244	1,057,244
MCap/ Sales (x)	6.6	4.7	8.0	6.6
EV (₹ Mn.)	497,600	490,017	1,013,377	965,338
EV/Sales (x)	6.2	4.4	7.6	6.0
EV/EBDITA (x)	15.2	9.9	17.4	14.1
P/BV (x)	4.7	4.1	7.6	5.9
Dividend Yield (%)	0.8	0.9	0.9	0.9

E-estimates

BUY	Upside above 20%
ACCUMULATE	Upside above 5% and up to 20%
REDUCE	Upside of upto 5% or downside of upto 15%
SELL	Downside of more than 15%

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