

ADD

Dishman Pharmaceuticals & Chemicals

Target Price (INR)

52

Confidence yet to flow, but operating leverage can deliver

Rating

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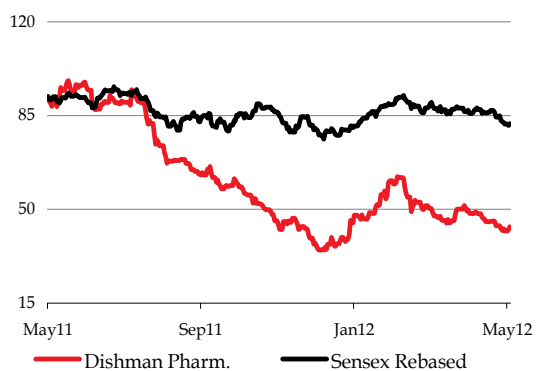
Last Price (INR)

43.5

Bloomberg code	DISH IN
Reuters code	DISH.Bo
Avg. Vol. (3m)	286,625
Avg. Val.(3m)(INRmn)	14.7
52-wk H/L (INR)	103 / 32.5
Sensex	16,328
MCAP (INRbn/USDmn)	3.51 / 65.2

Shareholding (%)	12/11	03/12
Promoters	61.4	61.4
MFs, FIs, Banks	7.4	6.4
FIIIs	3.3	3.3
Public	9.8	11.6
Others	18.2	17.4

Stock Chart (Relative to Sensex)



Stock Perf. (%)	1m	3m	1yr
Absolute	-10.3	-27.3	-52.0
Rel. to Sensex	-5.8	-17.0	-40.2

Financials (INRmn)	03/12	03/13f	03/14f
Sales	11,221	12,069	13,258
YoY (%)	13	8	10
EBITDA (%)	19.8	19.1	19.6
A.PAT	569	629	832
Sh o/s (diluted)	81	81	81
A.EPS (INR)	7.0	7.8	10.3
YoY (%)	-30	11	32
D/E (x)	0.8	0.6	0.5
P/E (x)	6.2	5.6	4.2
EV/E (x)	4.9	4.0	3.3
RoCE (%)	6	6	7
RoE (%)	6	7	9

Quarterly Trends	06/11	09/11	12/11	03/12
Sales (INRmn)	2,372	2,692	2,655	3,502
PAT (INRmn)	151	(63)	167	313

DISH's PAT performance during the Mar12 quarter, stood its best since the Dec09 quarter, with flattish revenues on a reasonably large base and expansion in operating margins. The MM business fell 14% during the quarter, nevertheless clocking in a third of annual revenues, courtesy increased Vitamin D3 sales. On a series of pipeline projects, the management appears confident of delivering growth; FY13f budgeted sales target stands at INR1.25bn, and a PAT target of INR1bn. After bouncing a few assets in and out of plans, the volatility in deciding their viability may put investors at a discomfort. However, valuations look compellingly reasonable and operating leverage can propel a surprise. We rollover our TP to Mar13 and lower it to INR52; upgrade to Add.

Revenue growth on noticeable base, PAT highest since Dec09

DISH reported a 2% revenue growth during the Mar12 quarter (unaudited numbers) on a reasonably large base of Mar11. Revenue from the CRAMS segment rose 14% y-o-y, a combination of a decline at Carbogen Amcis (CA) on the one hand, set off by a sharp growth in domestic operations on the other. The MM business fell 14% during the quarter, nevertheless clocking in a third of annual revenues, courtesy the increased Vitamin D3 sales on a shortage situation globally, according to the management. The fickle nature of the opportunity is thus difficult to ignore. PAT at INR313mn during the quarter stood its best since the Dec09 quarter.

Company remains optimistic on project line ups, execution is key

Across businesses, DISH remains optimistic on its project pipeline. The HiPo plant, for example, has been audited by various MNCs and revenues are expected to tick in. With Eisai Co Ltd (4523 JP, NR), CA is developing a prostrate cancer molecule, currently in an advanced phase of development. According to the company, an EU-based disinfectant major is in talks with the company to form a JV, possibly extending into a stake sale at a future date. While the euphoria is being sounded, execution is yet to be seen.

Backtracking on asset use hampers confidence...

Over the last 12 months, DISH has gone back and forth on its plans for its Chinese unit. The USD20mn asset was facing problems in securing local regulatory approvals and the company decided to put the unit on the block. Now, in the absence of a buyer plans of bringing the plant back to operations have revived. A SEZ into which DISH invested is also now being planned to be de-notified. The volatility in deciding the viability and mere existence of assets is likely to stroke discomfort among investors.

... but operating leverage could propel surprise; upgrade to Add

At 5.6x/4.2x the FY13f/FY14f EPS, valuations seem compellingly reasonable. Operating leverage can propel a surprise, and a stronger-than-estimated revenue growth could have a disproportionate positive impact on earnings. We rollover our TP to Mar13 and lower it to INR52; upgrade to Add. Lower-than-estimated sales from India CRAMS and CA are a risk.

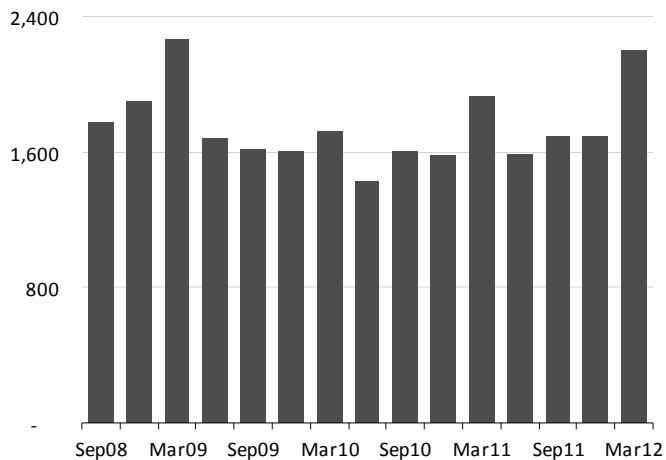
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Exhibit 1: Mar12 quarter financial snapshot

(INRmn)	Mar11 (3m)	Dec11 (3m)	Q-o-q (%)	Mar12 (3m)	Y-o-y (%)
Total operating income	3,444.0	2,654.6	31.9%	3,501.9	1.7%
Total operating expenses	2,889.2	2,046.8		2,677.4	
EBITDA	554.9	607.8	35.7%	824.5	48.6%
Other income	33.9	7.3		95.3	
Depreciation	187.5	191.1		180.5	
EBIT	401.3	424.0	74.4%	739.3	84.2%
Interest	104.8	164.0		217.7	
Recurring PBT	296.5	260.0	100.7%	521.6	75.9%
Net extraordinary items	-	-		-	
PBT (reported)	296.5	260.0		521.6	75.9%
Total taxes	67.1	92.7		208.3	
PAT (reported)	229.5	167.2	87.3%	313.3	36.6%
(+) Share in assoc. earnings	-	-		0.00	
Less: Minority interest	-	-		-	
Prior period items	-	-		-	
Net income (reported)	229.5	167.2		313.3	36.6%
Shares outstanding (mn)	80.7	80.7		80.7	
EPS (INR)	2.8	2.1		3.9	
Operating ratios					
EBITDA margin	16.1%	22.9%		23.5%	
EBIT margin	11.7%	16.0%		21.1%	
Net profit margin	6.7%	6.3%		8.9%	
Revenue breakdown					
CRAMS	1,930.4	1,691.1	30.0%	2,197.7	13.8%
MM	1,513.7	963.5	35.4%	1,304.2	-13.8%

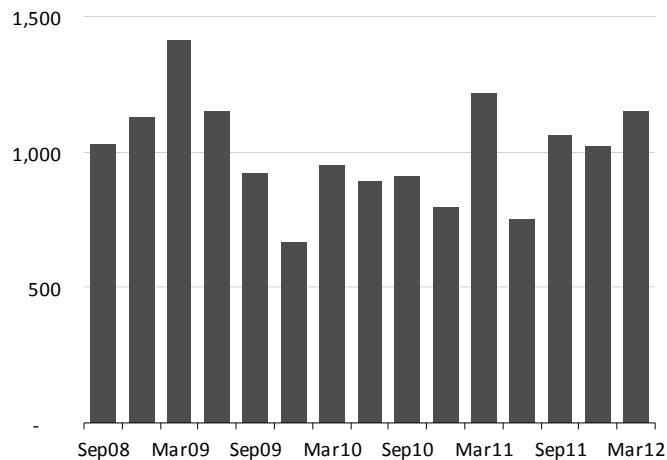
Source: Company, Avendus Research

Exhibit 2: CRAMS revenues (INRmn)



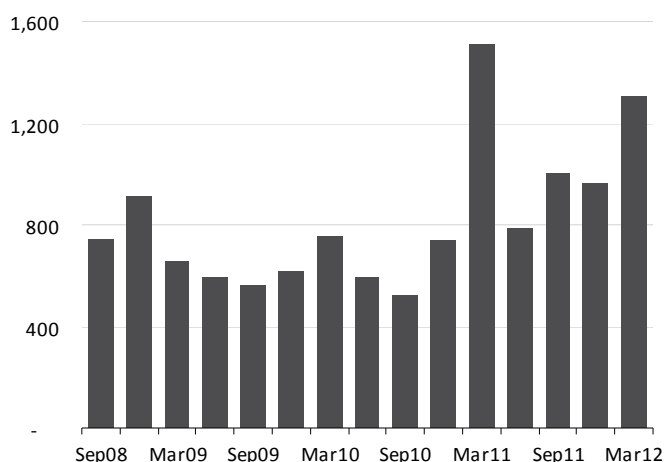
Source: Company, Avendus Research

Exhibit 3: CA revenues (INRmn)



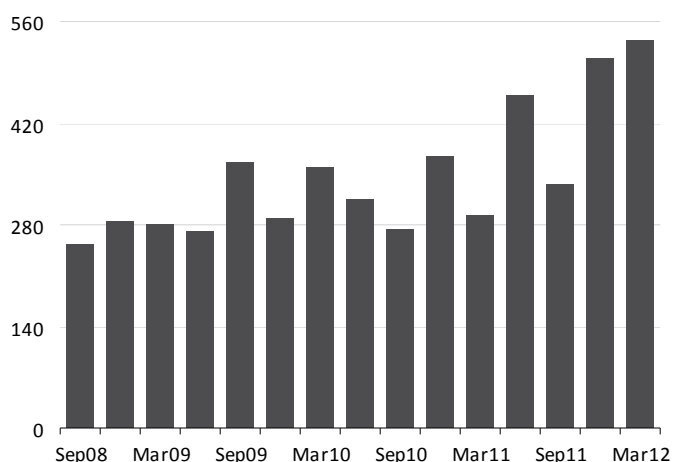
Source: Company, Avendus Research

Exhibit 4: MM revenues (INRmn)



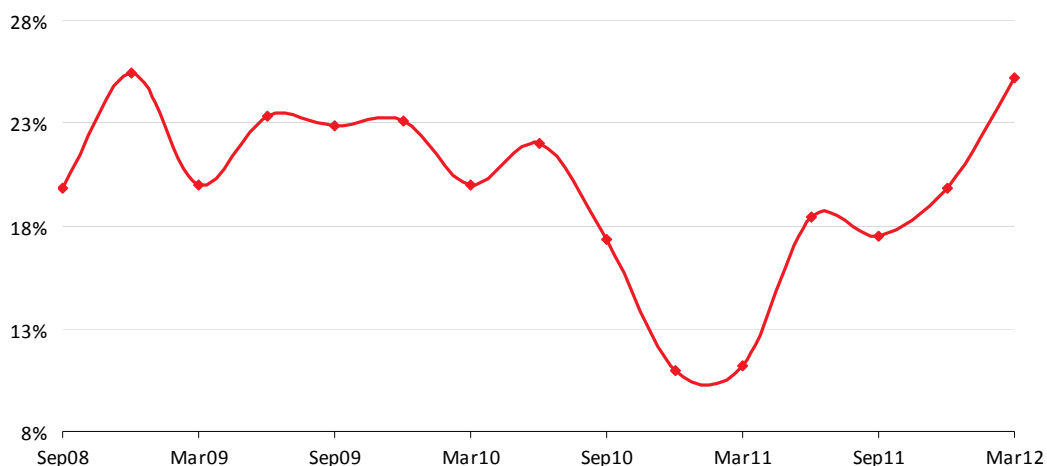
Source: Company, Avendus Research

Exhibit 5: Dishman Netherlands revenues (INRmn)



Source: Company, Avendus Research

Exhibit 6: EBITDA margin trend (adjusted for forex)



Source: Company, Avendus Research

Key takeaways from analyst call

- ▶ Overall, DISH has budgeted revenues of INR12.5bn in FY13f (which would mark a c11% y-o-y growth) with an EBITDA guidance of 21%. The budgeted PAT for FY13f is INR1bn.
- ▶ The Vitamin D business contributed INR500mn to the revenues during the quarter. For the full year, it contributed INR1.9bn to sales (INR1.2bn in FY11). Vitamin D3 is in short supply worldwide, as a result of which prices shot up c50%.
 - Margins in the MM segment improved during the quarter due to the change in the product mix and price increases in select molecules.
- ▶ CA reported revenues of CHF73mn for FY12. The company believes that the issues relating to CA are taken care of now. The revenue guidance for CA came in at CHF85–90mn in FY13f with an EBITDA target of CHF8mn.
 - CA is currently booked for 70% of its capacity, according to the company.
- ▶ DISH has not been able to find a suitable buyer for its facility in China and now plans to begin operations in this facility. It is in discussions with a CMO for a strategic partnership. It has guided for a turnover of USD5mn in FY13f from this plant.

- ▶ Revenues from the contract with Abbott Laboratories (ABT US, NR) for supply of Eprosartan are expected to rise 10–15% in FY13f.
- ▶ The HiPo plant is currently operating at 20% utilization and is expected to commercialize its first product from Jun12. DISH intends to double the capacity of this plant over FY13–14f. At 2x times its current capacity, the plant is expected to generate revenues of USD30–40mn.
- ▶ The new units for disinfectants, oncology (HiPo) and vitamin D3 are fully operational, according to the company. Some details on project line ups are as follows:
 - DISH is enthused about the interest that the HiPo unit is generating among potential clients.
 - The company is in discussions with an EU-based major disinfectant manufacturing company entering into a JV for the disinfectant unit. According to the management, the discussions include a prospect of a stake sale at a future date.
 - CA is currently developing a prostate cancer drug for Eisai Co, which is in phase III clinical trials.
- ▶ The consolidated debt stood at INR8.9bn at the end of FY12; cUSD20mn is due for repayment in FY13f. The company had cash and equivalents of cINR300–400mn at the end of FY12.
- ▶ DISH invested cINR1bn in acquiring land in a SEZ. However, it now plans to de-notify the SEZ and realize its invested amount by selling this land.
- ▶ The company's tax rate guidance for FY13f is 23–24% and capex guidance is INR300–400mn.

Exhibit 7: Change in estimates

(INRmn)	FY13f			FY14f			FY15f
	Old	New	Change (%)	Old	New	Change (%)	
Revenues	11,647	12,069	3.6	13,019	13,258	1.8	14,620
EBITDA	2,262	2,310	2.1	2,643	2,598	-1.7	2,922
PAT	642	629	-2.0	856	832	-2.7	1,093

Source: Avendus Research

We value DISH at 5x the Mar14 EPS, which is a c40% discount to the average one-year forward rolling multiple over the last 12 months.

Exhibit 8: One-year forward rolling P/E and P/E at TP



Source: Bloomberg, Avendus Research

Risk factors

- ▶ Lower-than-expected performance in the domestic CRAMS operations and CA is a risk to our call.
- ▶ We have not assumed revenue growth in the eprosartan sales to ABT, contrary to the company's guidance, which could provide an upside to earnings.

Financials and Valuations

Income statement (INRmn)

Fiscal year ending	03/12	03/13f	03/14f	03/15f
Total operating income	11,221	12,069	13,258	14,620
Total operating expenses	8,996	9,760	10,661	11,698
EBITDA	2,225	2,310	2,598	2,922
Other income	150	42	46	49
Depreciation	765	799	823	838
EBIT	1,610	1,553	1,821	2,134
Interest	729	733	733	705
Recurring PBT	880	820	1,088	1,429
Net extra ordinary items	0	0	0	0
PBT (reported)	880	820	1,088	1,429
Total taxes	312	191	256	336
PAT (reported)	569	629	832	1,093
(+) Share in assoc. earnings	0	0	0	0
Less: Minority interest	0	0	0	0
Prior period items	0	0	0	0
Net income (reported)	569	629	832	1,093
Aventus net income	569	629	832	1,093
Shares outstanding (mn)	81	81	81	81
Aventus dil. shares (mn)	81	81	81	81
Aventus EPS (INR)	7.0	7.8	10.3	13.5

Growth ratios (%)

Total operating income	13.2	7.6	9.9	10.3
EBITDA	36.9	3.8	12.5	12.5
EBIT	20.4	-3.5	17.2	17.2
Recurring PBT	-4.4	-6.8	32.6	31.4
Aventus net income	-30.1	10.7	32.2	31.4
Aventus EPS	-30.1	10.7	32.2	31.4

Operating ratios (%)

EBITDA margin	19.8	19.1	19.6	20.0
EBIT margin	14.3	12.9	13.7	14.6
Net profit margin	5.0	5.2	6.3	7.5
Other income/PBT	17.1	5.2	4.2	3.5
Effective Tax rate	35.4	25.3	24.5	24.5

Balance sheet (INRmn)

Fiscal year ending	03/12	03/13f	03/14f	03/15f
Equity capital	161	161	161	161
Preference capital	-	-	-	-
Reserves and surplus	8,651	9,051	9,715	10,668
Net worth	8,812	9,213	9,876	10,829
Minority interest	-	-	-	-
Total debt	8,964	9,352	8,965	8,655
Deferred tax liability	323	372	437	523
Total liabilities	18,098	18,936	19,278	20,007
Gross block	16,322	16,822	17,322	17,822
less: Acc. depreciation	4,044	4,843	5,666	6,503
Net block	12,279	11,979	11,657	11,319
CWIP	1,500	500	500	500
Goodwill	77	77	77	77
Investments	14	14	14	14
Cash	102	1,986	2,217	2,800
Inventories	3,158	3,221	3,542	3,877
Debtors	1,998	2,149	2,361	2,604
Loans and advances	1,844	1,984	2,179	2,403
less: Current liabilities	2,105	2,147	2,362	2,584
less: Provisions	769	827	908	1,001
Net working capital	4,229	6,366	7,030	8,098
Total assets	18,098	18,936	19,278	20,007

Cash flow statement (INRmn)

Fiscal year ending	03/12	03/13f	03/14f	03/15f
Net profit	569	613	821	1,079
Depreciation	765	799	823	838
Deferred tax	0	49	65	86
Working capital changes	-835	-114	-238	-261
Less: Other income	150	42	46	49
Cash flow from operations	349	1,305	1,426	1,693
Capital expenditure	-384	500	-500	-500
Strategic investments	0	0	0	0
Marketable investments	0	0	0	0
Change in other loans & adv.	-165	-140	-195	-224
Goodwill paid	0	0	0	0
Other income	150	42	46	49
Cash flow from investing	-398	403	-650	-674
Equity raised	0	0	0	0
Change in borrowings	275	388	-387	-310
Dividends paid (incl. tax)	-113	-113	-113	-113
Others	-435	-100	-45	-13
Cash flow from financing	-273	176	-545	-435
Net change in cash	-323	1,884	231	583

Key Ratios

Fiscal year ending	03/12	03/13f	03/14f	03/15f
Valuation ratios (x)				
P/E (on Aventus EPS)	6.2	5.6	4.2	3.2
P/E (on basic, reported EPS)	6.2	5.6	4.2	3.2
P/CEPS	2.6	2.5	2.1	1.8
P/BV	0.4	0.4	0.4	0.3
Dividend yield (%)	2.8	2.8	2.8	2.8
Market cap. / Sales	0.3	0.3	0.3	0.2
EV/Sales	1.0	0.8	0.6	0.5
EV/EBITDA	4.9	4.0	3.3	2.6
Net Cash / Market cap.	55.5	113.1	125.2	148.2
Per share ratios (INR)				
Aventus EPS	7.0	7.8	10.3	13.5
EPS (Basic, reported)	7.0	7.6	10.2	13.4
Cash EPS	16.5	17.7	20.5	23.9
Book Value	109.2	114.2	122.4	134.2
Dividend per share	1.2	1.2	1.2	1.2
Total assets / equity (x)	2.0	2.1	2.0	1.9
Return ratios (%)				
ROCE	5.8	6.4	7.3	8.3
ROIC	7.0	7.1	8.4	9.8
ROE	6.5	7.0	8.7	10.6
ROA	3.2	3.4	4.4	5.6
OCF/Sales	3.1	10.8	10.8	11.6
FCF/Sales	-0.3	15.0	7.0	8.2
Turnover ratios (x)				
Asset turnover (x)	0.6	0.7	0.7	0.7
Gross asset turnover	0.7	0.7	0.8	0.8
Inventory / Sales (days)	95.3	96.4	93.1	92.6
Receivables (days)	60.7	62.7	62.1	62.0
Payables (days)	228.4	154.3	148.8	149.6
Working capital cycle (days)	60.7	70.7	69.2	69.0
Solvency ratios (x)				
Gross debt to equity	1.1	1.1	1.0	0.8
Net debt to equity	0.8	0.6	0.5	0.4
Net debt to EBITDA	4.0	4.0	3.5	3.0
Interest Coverage (on EBIT)	2.2	2.1	2.5	3.0

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Proportion of ratings in each category and investment banking relationships												
At the end of March 2012						Buy	Add	Hold	Reduce	Sell	NR	Total
Proportion of ratings in each category						29.1	33.3	17.4	11.6	1.4	7.2	100.0
Proportion of companies to whom material investment banking services were offered during the previous 12 months						0.0	8.7	8.3	0.0	0.0	20.0	5.8

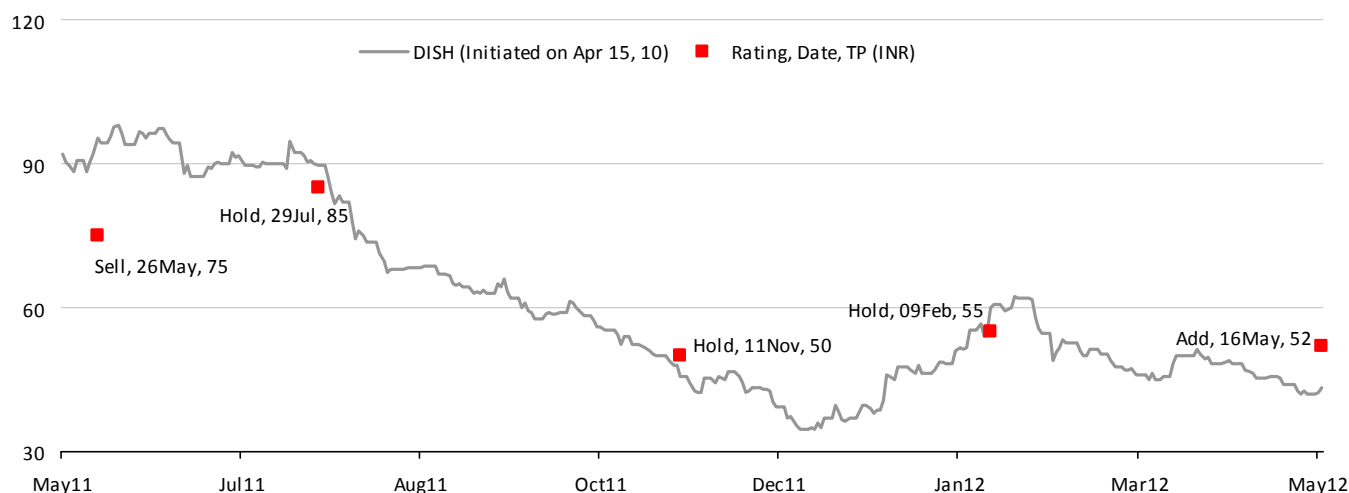
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