

Novartis India Limited

CMP Rs. 565.0
BUY

Q3FY10
Result Update

Novartis India Ltd. (NIL), the listed subsidiary of Swiss drug maker Novartis AG, posted a marginal decline of 4.2% Y-o-Y in Reported PAT to Rs. 231.5 Mn. for the quarter ended December 2009, against Rs. 241.7 Mn. for the same quarter last year. Net Revenues for Q3FY10 stood at Rs. 1,604.6 Mn., growing by about 2% Y-o-Y. Employee Costs & Other Expenses increased by more than 23% & 14% respectively, leading to a decline of 34% in Operating Profits to Rs. 158.3 Mn. Operating Margins too declined to 10% in Q3FY10 vis-à-vis 15.3% in Q3FY09. Other Income increased from Rs. 178.3 Mn. in Q3FY09 to Rs. 217.4 Mn. in Q3FY10. However, NIL witnessed a significant drop in Interest outflow of more than 85% Y-o-Y. Effective Tax Rate for the quarter ended December 2009 stood at 37.3% as against 40.6% in the same period last year.

On a sequential basis, Novartis reported dismal set of numbers for the third quarter of FY2010. The company's topline dipped marginally to Rs. 1,604.6 Mn. in Q3FY10 against Rs. 1,615.4 Mn. in Q2FY10. With a 16% Q-o-Q increase in Total Expenditure, NIL witnessed a sharp decline of almost 52% in Operating Profits for Q3FY10. Operating Margins declined sharply by over 10%. However, the pharmaceutical company saw its Other Income increase by 20% Q-o-Q to Rs. 217.4 Mn. from Rs. 181.2 Mn. in Q2FY10. A decline of close to 20% Q-o-Q in Current Tax helped the company, curb the decline in its bottomline. NIL reported Net Profit of Rs. 231.5 Mn. for the quarter ended December 2009, as against Rs. 332.6 Mn. reported in the previous quarter, a decline of over 30% Q-o-Q. EPS for Q3FY10 stood at Rs. 7.2.

For the first nine months of FY2010, Novartis India Ltd. reported a 2.2% increase in its topline to Rs. 4,751.8 Mn. from Rs. 4,651.0 Mn. in the corresponding period last year. The bottomline too increased by 6.2% Y-o-Y to Rs. 881.7 Mn. EPS for nine months ended December 2009 stood at Rs. 27.6.

Segmental Revenues								
Particulars (Rs Mn)	Q3FY10	Q2FY10	Q-Q(%)	Q3FY09	Y-Y(%)	9MFY10	9MFY09	Y-Y(%)
Pharmaceuticals	1,098.1	1,135.0	-3.3%	1,010.0	8.7%	3,359.3	3,114.9	7.8%
OTC	250.3	207.0	20.9%	233.1	7.4%	626.8	630.0	-0.5%
Animal Health	158.6	173.7	-8.7%	124.1	27.8%	460.5	372.6	23.6%
Generics	97.6	99.7	-2.1%	202.1	-51.7%	305.2	533.5	-42.8%
Total	1,604.6	1,615.4	-0.7%	1,569.3	2.2%	4,751.8	4,651.0	2.2%

The Pharmaceutical division of Novartis India Ltd. reported stable growth of 7.8% Y-o-Y for the first nine months ended December 2009. However, the Generics business still remains under pressure & registered a decline of close to 43% Y-o-Y. The company has been able to report good improvement in Animal Health business that grew by more than 23% Y-o-Y.

Recent Updates

- In a recent development, Swiss pharma major - Novartis AG made an announcement to increase its stake in the world's largest eye-care company – Alcon from 25% to 77%, by exercising its call option to buy additional 52% from Nestle for USD 28.1 billion. Novartis and Alcon have highly complementary product portfolios covering more than 70% of global vision care sector. After completing the 77% stake buy from Nestle & subsequently entering into an all-share direct merger with Alcon for the remaining 23% minority stake, the pharma major proposes to merge Alcon with itself. Post this merger, the new eye-care division of Novartis AG would include Alcon, Ciba Vision & selected ophthalmic medicines.

The global Eye-care leader – Alcon, has a 100% subsidiary in India named Alcon India Ltd. located at Bangalore. If Novartis' takeover of Alcon goes through seamlessly & eventually results in an integration of Alcon India into its Indian arm, i.e Novartis India Ltd., the Swiss pharma giant could break into the league of top five players in the Rs. 600 crore plus Indian eye-care market. This would be a huge positive for the Indian listed entity.

2. In another positive boost for Novartis, its anti-cancer drug – 'Nilotinib' has been granted patent protection in India in December 2009. Nilotinib is a superior version of its blood cancer drug Glivec (imatinib mesylate), for which the company has been engaged in a legal battle with the Government on the latter's decision to deny patent protection for Glivec. Novartis markets Nilotinib globally as Tasigna, which is used as the second-line therapy for Glivec-resistant patients in case of chronic myelogenous leukemia. The drug was approved in the US three years ago.

We believe that these developments are positive for Novartis India Ltd. & would help the company achieve better growth in the future.

Valuations

Looking at the recent developments, we continue to remain positive about the future prospects for this MNC pharmaceutical company. Novartis India is a debt-free & cash rich company with Cash & Cash Equivalents (CCE) of Rs. 140 per share, as of March 2009. (Cash Equivalents refer to the Inter Corporate Deposits). The company has also maintained a dividend per share of Rs. 10 for the past few years on a face value of Rs. 5 per share.

However, taking into account the dismal performance for the third quarter, we have revised our full year FY10 estimates downward to Rs. 37 vis-à-vis Rs. 39.3 earlier. At CMP of Rs. 565.0, the scrip trades at 15.3x our revised earnings of Rs. 37 for FY10E. Maintain BUY.

Quarterly Financials

Earnings Statement								
YE March (Rs. Mn.)	Q3FY10	Q2FY10	Q-Q(%)	Q3FY09	Y-Y(%)	9MFY10	9MFY09	Y-Y(%)
Net Revenues	1,604.6	1,615.4	-0.7%	1,569.3	2.2%	4,751.8	4,651.0	2.2%
Cost of Materials	672.7	619.4	8.6%	668.9	0.6%	1,898.5	1,884.4	0.7%
Gross Profit	931.9	996.0	-6.4%	900.4	3.5%	2,853.3	2,766.6	3.1%
Staff Costs	244.7	200.1	22.3%	198.2	23.5%	645.2	538.8	19.7%
Other Expenses	528.9	466.9	13.3%	462.4	14.4%	1,400.9	1,319.7	6.2%
Total Expenditure	773.6	667.0	16.0%	660.6	17.1%	2,046.1	1,858.5	10.1%
Operating Profit	158.3	329.0	-51.9%	239.8	-34.0%	807.2	908.1	-11.1%
OPM (%)	9.9%	20.4%	(1,050.1)	15.3%	(541.5)	17.0%	19.5%	(253.8)
Other Income	217.4	181.2	20.0%	178.3	21.9%	587.9	498.7	17.9%
EBITDA	375.7	510.2	-26.4%	418.1	-10.1%	1,395.1	1,406.8	-0.8%
Depreciation	5.6	5.6	0.0%	6.5	-13.8%	16.8	20.1	-16.4%
EBIT	370.1	504.6	-26.7%	411.6	-10.1%	1,378.3	1,386.7	-0.6%
Interest	0.7	0.5	40.0%	4.8	-85.4%	1.9	6.3	-69.8%
PBT	369.4	504.1	-26.7%	406.8	-9.2%	1,376.4	1,380.4	-0.3%
Tax	137.9	171.5	-19.6%	165.1	-16.5%	494.7	550.4	-10.1%
<i>Current Tax</i>	149.9	187.5	-20.1%	156.3	-4.1%	513.4	521.5	-1.6%
<i>Fringe Benefit Tax</i>	0.0	(10.6)		13.7		0.0	38.6	
<i>Deferred Tax</i>	(12.0)	(5.4)	122.2%	(4.9)	144.9%	(18.7)	(9.7)	92.8%
PAT	231.5	332.6	-30.4%	241.7	-4.2%	881.7	830.0	6.2%
Equity Capital	159.8	159.8		159.8		159.8	159.8	
EPS	7.2	10.4	-30.4%	7.6	-4.2%	27.6	26.0	6.2%
Ratio Analysis								
Profitability								
YE March	Q3FY10	Q2FY10	Q-Q(%)	Q3FY09	Y-Y(%)	9MFY10	9MFY09	Y-Y(%)
OPM (%)	9.9%	20.4%	(1,050.1)	15.3%	(541.5)	17.0%	19.5%	(253.8)
EBITDA (%)	23.4%	31.6%	(817.0)	26.6%	(322.9)	29.4%	30.2%	(88.8)
EBIT (%)	23.1%	31.2%	(817.2)	26.2%	(316.3)	29.0%	29.8%	(80.9)
PAT (%)	14.4%	20.6%	(616.2)	15.4%	(97.4)	18.6%	17.8%	70.9
Operational Parameters								
YE March	Q3FY10	Q2FY10	Q-Q(%)	Q3FY09	Y-Y(%)	9MFY10	9MFY09	Y-Y(%)
RM Consumed	41.9%	38.3%	358.0	42.6%	(70.1)	40.0%	40.5%	(56.3)
Staff Cost	15.2%	12.4%	286.3	12.6%	262.0	13.6%	11.6%	199.3
Other Expenditure	33.0%	28.9%	405.8	29.5%	349.6	29.5%	28.4%	110.7
Effective Tax Rate	37.3%	34.0%	331.0	40.6%	(325.4)	35.9%	39.9%	(393.1)

Financials

Earnings Statement								
Particulars (Rs. Mn.)	FY05	FY06	FY07	FY08	FY09	FY10E	FY11E	FY12E
Total Revenues	4,714.9	5,259.2	5,422.4	5,534.5	5,994.8	6,315.8	6,761.1	7,239.3
- Growth (%)		11.5%	3.1%	2.1%	8.3%	5.4%	7.0%	7.1%
Total Expenditure	4,008.7	4,397.4	4,536.7	4,546.2	4,880.7	5,240.4	5,596.5	5,978.9
Operating Profit	706.3	861.8	885.6	988.3	1,114.1	1,075.4	1,164.6	1,260.4
Forex Gain/(Loss)	1.4	(0.4)	3.2	3.7	(11.1)	0.0	0.0	0.0
Other Income	402.3	634.5	497.5	585.7	660.0	770.2	806.0	851.5
EBITDA	1,109.9	1,495.9	1,386.4	1,577.7	1,763.1	1,845.6	1,970.6	2,111.9
Depreciation	52.2	5.9	26.7	28.5	26.9	24.8	26.8	28.8
EBIT	1,057.8	1,469.4	1,380.2	1,549.2	1,736.2	1,820.8	1,943.8	2,083.1
Interest	17.4	26.5	6.3	6.0	7.1	1.9	0.0	0.0
PBT	1,040.4	1,463.6	1,353.5	1,543.1	1,729.1	1,818.9	1,943.8	2,083.1
Tax	389.2	410.3	468.0	570.8	692.0	636.6	680.3	729.1
PAT Before EI	651.2	1,053.3	885.5	972.3	1,037.1	1,182.3	1,263.5	1,354.0
- Growth (%)		61.8%	-15.9%	9.8%	6.7%	14.0%	6.9%	7.2%
Extra-ordinary Items	0.0	25.6	0.0	0.0	0.0	0.0	0.0	0.0
PAT	651.2	1,078.9	885.5	972.3	1,037.1	1,182.3	1,263.5	1,354.0

Ratio Analysis								
Particulars	FY05	FY06	FY07	FY08	FY09	FY10E	FY11E	FY12E
OPM (%)	15.0%	16.4%	16.3%	17.9%	18.6%	17.0%	17.2%	17.4%
EBITDA (%)	23.5%	28.4%	25.6%	28.5%	29.4%	29.2%	29.1%	29.2%
PBIT (%)	22.4%	27.9%	25.5%	28.0%	29.0%	28.8%	28.7%	28.8%
PAT (%)	13.8%	20.5%	16.3%	17.6%	17.3%	18.7%	18.7%	18.7%
Interest Cover (x)	60.9	55.5	220.8	256.2	246.0	958.3	-	-
EPS (Rs.)	20.4	33.8	27.7	30.4	32.4	37.0	39.5	42.4
P/E (x)	27.7	16.7	20.4	18.6	17.4	15.3	14.3	13.3
P/BV (x)	6.4	5.3	4.6	4.0	3.5	3.0	2.6	2.3
BVPS (Rs.)	89.0	105.6	121.6	140.3	161.1	186.3	214.2	244.8
Market Cap (Rs. Mn.)	18,057.9	18,057.9	18,057.9	18,057.9	18,057.9	18,057.9	18,057.9	18,057.9
M Cap/Sales (x)	3.8	3.4	3.3	3.3	3.0	2.9	2.7	2.5
EV (Rs. Mn.)	17,479.4	16,862.4	18,096.8	17,910.2	17,523.3	17,366.7	16,809.5	16,184.9
EV/EBITDA (x)	15.7	11.3	13.1	11.4	9.9	9.4	8.5	7.7
EV/Sales (x)	3.7	3.2	3.3	3.2	2.9	2.7	2.5	2.2
ROCE (%)	36.3%	42.7%	34.7%	34.5%	33.7%	30.6%	28.4%	26.6%
RONW (%)	22.9%	31.2%	22.8%	21.7%	20.1%	19.9%	18.5%	17.3%
Debt/Equity Ratio (x)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Inventory T/o Days	51.0	42.6	45.4	44.6	30.5	40.0	40.0	40.0
Debtors T/o Days	32.2	27.5	28.6	26.0	27.7	28.0	28.0	28.0
Advances T/o Days	121.2	154.1	232.4	274.3	288.6	295.0	295.0	295.0
Creditors T/o Days	56.1	48.1	45.3	47.9	54.3	51.0	51.0	51.0
Working Cap T/o Days	165.0	219.3	249.8	266.9	285.6	317.9	345.4	372.4
Fixed Assets T/o (Gross)	3.1	23.5	23.4	23.7	26.3	25.5	25.2	25.1
DPS (Rs.)	10.0	15.0	10.0	10.0	10.0	10.0	10.0	10.0
Dividend Payout (%)	49.1%	44.4%	36.1%	32.9%	30.8%	27.0%	25.3%	23.6%
Dividend Yield (%)	1.8%	2.7%	1.8%	1.8%	1.8%	1.8%	1.8%	1.8%

Financials

Balance Sheet								
Particulars (Rs. Mn.)	FY05	FY06	FY07	FY08	FY09	FY10E	FY11E	FY12E
Equity Capital	159.8	159.8	159.8	159.8	159.8	159.8	159.8	159.8
Reserves	2,683.9	3,216.2	3,726.0	4,324.4	4,987.6	5,796.0	6,685.5	7,665.6
Shareholders Funds	2,843.7	3,376.0	3,885.8	4,484.2	5,147.4	5,955.8	6,845.3	7,825.4
Minority Interest								
Borrowed Funds	69.0	63.1	92.0	4.4	3.0	0.0	0.0	0.0
Deferred Tax Liability	(86.1)	(108.1)	(132.1)	(128.4)	(138.9)	(138.9)	(138.9)	(138.9)
Total Liabilities	2,826.6	3,331.0	3,845.7	4,360.2	5,011.5	5,816.9	6,706.4	7,686.5
Fixed Assets	219.8	100.8	96.7	93.5	86.9	81.4	74.6	65.8
Investments	475.3	70.8	37.7	220.1	233.9	233.9	233.9	233.9
Current Assets								
Inventory	658.6	613.2	674.0	676.6	501.0	692.1	740.9	793.3
Sundry Debtors	415.9	396.1	424.2	393.8	454.9	484.5	518.7	555.3
Other Current Assets	0.8	0.8	0.8	0.8	0.0	0.0	0.0	0.0
Loans & Advances	1,565.6	2,219.8	3,452.4	4,158.7	4,740.0	5,104.6	5,464.4	5,850.9
Cash & Bank Balance	647.5	1,258.6	53.1	152.0	537.5	691.1	1,248.3	1,873.0
Current Liabilities								
Sundry Creditors	724.6	692.8	673.1	726.8	892.4	882.5	944.7	1,011.5
Provisions	432.4	636.4	220.1	608.3	650.4	588.3	629.8	674.3
Net Current Assets	2,131.5	3,159.5	3,711.4	4,046.7	4,690.7	5,501.5	6,397.9	7,386.7
Miscellaneous Expenditure								
Total Assets	2,826.6	3,331.0	3,845.7	4,360.2	5,011.5	5,816.9	6,706.4	7,686.5

Cash Flow								
Particulars (Rs. Mn.)	FY05	FY06	FY07	FY08	FY09	FY10E	FY11E	FY12E
Opening Cash & Bank	86.6	647.5	1,258.6	53.1	152.0	537.5	691.1	1,248.3
Profit After Tax	651.2	1,078.9	885.5	972.3	1,037.1	1,182.3	1,263.5	1,354.0
Investment Income	(402.3)	(634.5)	(497.5)	(585.7)	(660.0)	(770.2)	(806.0)	(851.5)
Interest Paid	17.4	26.5	6.3	6.0	7.1	1.9	0.0	0.0
Miscellaneous Exp W/Off	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Depreciation	52.2	5.9	26.7	28.5	26.9	24.8	26.8	28.8
Deferred Taxation	90.3	(22.0)	(18.3)	3.7	(10.5)	0.0	0.0	0.0
Others	(189.3)	(1,192.1)	(22.6)	(22.2)	(26.8)	0.0	0.0	0.0
Change in Working Cap	312.7	(416.9)	(1,757.5)	(236.4)	(258.4)	(657.3)	(339.1)	(364.2)
CF - Operating Activities	532.2	(1,154.2)	(1,377.4)	166.4	115.4	(218.5)	145.1	167.1
Change in Fixed Assets	64.7	1,305.3	(5.7)	(3.1)	6.4	(19.3)	(20.0)	(20.0)
Change in Investments	(64.7)	404.5	33.1	(182.4)	(13.9)	0.0	0.0	0.0
Investment Income	402.3	634.5	497.5	585.7	660.0	770.2	806.0	851.5
CF - Investing Activities	402.3	2,344.3	524.9	400.1	652.5	750.8	786.0	831.5
Increase in Equity	0.0	0.0	(11.2)	(0.0)	(0.0)	(0.0)	(0.0)	0.0
Changes in Borrowings	9.0	(5.9)	28.9	(87.6)	(1.4)	(3.0)	0.0	0.0
Interest Paid	(17.4)	(26.5)	(6.3)	(6.0)	(7.1)	(1.9)	0.0	0.0
Dividend Paid	(365.3)	(546.7)	(364.4)	(373.9)	(373.9)	(373.9)	(373.9)	(373.9)
CF - Financing Activities	(373.7)	(579.0)	(353.0)	(467.6)	(382.4)	(378.8)	(373.9)	(373.9)
Net Change in Cash	560.8	611.2	(1,205.5)	98.9	385.5	153.6	557.2	624.6
Closing Cash & Bank Balance	647.5	1,258.6	53.1	152.0	537.5	691.1	1,248.3	1,873.0

Disclaimer

Disclosure of Interest Statement

1. Analyst Ownership of the scrip
2. PPFAS ownership of the scrip
3. PMS ownership of the scrip

Novartis India Limited

NO
YES
YES

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