

Another deal from turnaround expert

growth prospects from Ranbaxy deal

FOLLOWING the announcement that Sun Pharma would acquire Ranbaxy, we upgrade Sun Pharma from Neutral to Buy with a revised P.O.(price objective) of ₹680 (24x FY16e).

Sun Pharma is to buy Ranbaxy for \$4 bn in an all share swap (16.2% dilution for Sun Pharma), valuing Ranbaxy at 2.2x TTM (last twelve months) sales. While the deal will be earnings dilutive in the near term (4% in FY16), we see significant synergies over the next

Per management, acquisition will be cash EPS accretive in the first-year. While our base cases for the first year are unchanged, given that today is unchanged, travelator, Sun Pharma's previous track record in M&A, we would expect the market to factor in some of this upside prior to the deal closure. When we moved up our PE (price-to-earnings) multiple to 2x (times) to reflect the higher growth visibility, which was a key reason for our earlier downgrade.

Acquired entity—Peak at regulatory issues, bottom of margins. We highlight that with all four US FDA approved plantaris under import alerts, Ranbaxy is at the peak of regulatory issues which has resulted sub optimal margins of 8% in CY13. We highlight that Ranbaxy spends 4% of its sales on consent decrees. While it is difficult to ascertain the regulatory time line, we believe there is significant scope for operational improvement and hence earnings upside.



	Sum Pharma (FY16)	Ranbaxy (FY16)	Sum Pharma (post-acquisition)
3 million			
Sales	2,209,046	1,35,986	3,45,034
EBITDA	87,463	11,612	99,075
EBITDA margins	41.89%	8.59%	28.70%
PAT	68,312	7904	76,216
EPS (₹)			31.7
Earnings dilution for Sum Pharma (FY16)			-4.00%

Source: BofA Merrill Lynch Global Research.

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The chart displays the performance of three trading strategies over time. The Y-axis represents a performance metric, likely a return or profit, ranging from 85 to 110. The X-axis shows the dates from January 13, 2014, to April 11, 2014. The three strategies are Sun Pharma, BSE Sensex, and Cipla. Sun Pharma shows the highest performance, peaking near 110. BSE Sensex and Cipla show lower performance, fluctuating between 90 and 105.

Sun Pharma has a history of turning around distressed assets, Sun Pharma has a successful track record of turning around distressed assets with recent cases such as Taro and URL. While we

acknowledge that Ranbaxy will likely have its own challenges, we highlight that Ranbaxy's gross margins (63-64%) are largely in line with other Indian peers (indicates that geography mix or prod-

The risks to our price objective are:

- (i) higher-than-expected price erosion in Taro portfolio,
- (ii) longer than anticipated turn-around time for Ranbaxy, (iii) higher price erosion in Doxil portfolio, and (iv) the possibility that the Ranbaxy acquisition does not consummate.

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