Panel Discussion

Healthcare Reform / Global M&A and Restructuring

Gideon Lo, Saion Mukherjee, David Stanton

June 2011
Australia – Key Healthcare metrics

Australian healthcare market is attractive

An ageing population will have sustained demand growth over longer term

- Australia’s aged population will continue to grow, due to a combination of increased life expectancy and lower birth rates.
- The proportion of the population older than 70 is around 9% in Australia. This figure is forecast to double over the next 40 years. An ageing population needs more tests and treatments.

Australian healthcare sector has high levels of IP

- Australian healthcare companies have high barriers to entry in the industries in which they compete
- The medical devices sector has a strong track record in innovation

Source: OECD data
Australia – current regulatory issues

Australia spends 8% of GDP on Healthcare

A new funding agreement between the Australian Government and the pathology industry has been signed – relevant for SHL AU and PRY AU

- The five-year agreement has a target growth rate of 4.98% pa for pathology spending
- We believe this agreement will lead to increased certainty for the Australian pathology industry, and the government is unlikely to introduce further reform over the medium term

Means-testing of the private insurance rebate – relevant for RHC AU

- Government will continue to try to phase out the 30% rebate once a couple’s income rises above A$160k
- We acknowledge that it is very difficult to forecast whether people will discontinue their PHI should this legislation be approved; we acknowledge the potential for people to leave PHI

Australia spends relatively less on healthcare

Healthcare expenditure as a % of GDP, 2008A

Source: OECD data
Australia – Our top picks

Australian Healthcare companies compete in niche industries

While Australian healthcare stocks compete in diverse industries, we believe the biggest driver of earnings of Australian healthcare companies relates to demand for medical services, which looks set to remain robust

Our Top picks are:
- **CSL AU** (BUY, PT A$43.55): a global plasma company with strong forecast growth
- **RMD AU** (BUY, PT A$4.23): an sleep apnoea company whose treatment taps into the global growth in obesity
- **COH AU** (BUY, PT A$88.00): a niche cochlear implant company with c70% market share
- **MSB AU** (BUY, PT A$10.45): an adult stem cell company whose treatments address a range of medical conditions

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## Stocks under coverage - Australia

<table>
<thead>
<tr>
<th>Company</th>
<th>Code</th>
<th>Rating</th>
<th>Price</th>
<th>Price target</th>
<th>Upside/downside (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ansell</td>
<td>ANN AU</td>
<td>Neutral</td>
<td>13.81</td>
<td>14.67</td>
<td>6.2</td>
</tr>
<tr>
<td>Clinuvel Pharmaceuticals</td>
<td>CUV AU</td>
<td>Buy</td>
<td>1.78</td>
<td>4.50</td>
<td>152.8</td>
</tr>
<tr>
<td>Cochlear</td>
<td>COH AU</td>
<td>Buy</td>
<td>80.03</td>
<td>88.00</td>
<td>10.0</td>
</tr>
<tr>
<td>CSL</td>
<td>CSL AU</td>
<td>Buy</td>
<td>33.55</td>
<td>43.55</td>
<td>29.8</td>
</tr>
<tr>
<td>iSOFT Group</td>
<td>ISF AU</td>
<td>Neutral</td>
<td>0.15</td>
<td>0.17</td>
<td>13.3</td>
</tr>
<tr>
<td>Mesoblast</td>
<td>MSB AU</td>
<td>Buy</td>
<td>8.02</td>
<td>10.45</td>
<td>30.3</td>
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<tr>
<td>Primary Health Care</td>
<td>PRY AU</td>
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<td>3.41</td>
<td>3.61</td>
<td>5.9</td>
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<tr>
<td>Ramsay Health Care</td>
<td>RHC AU</td>
<td>Neutral</td>
<td>18.1</td>
<td>18.35</td>
<td>1.4</td>
</tr>
<tr>
<td>ResMed Inc</td>
<td>RMD AU</td>
<td>Buy</td>
<td>2.96</td>
<td>4.32</td>
<td>45.9</td>
</tr>
<tr>
<td>Sonic Healthcare</td>
<td>SHL AU</td>
<td>Neutral</td>
<td>12.06</td>
<td>11.91</td>
<td>(1.2)</td>
</tr>
</tbody>
</table>

Pricing as at 26 May 2011
Source: Nomura estimates
China – key market dynamics

Healthy long-term growth, but slight policy headwinds

Neutral rating on the sector — healthy long-term but some short-term policy headwinds. Range-trading in 2011 – stock picks are increasingly important.

2011 is a major policy inflection year – cross-over of ongoing healthcare reform (2009-2011) and upcoming 12th Five-Year Plan (2011-15).

Sector correction has been driven by concern over risk of product price cuts and cost-inflation effects – operating de-leverage in 2011.

We think sector profit growth could slow to 15-20% y-y in 2011, from 2010’s circa 30%.

We expect a re-entry opportunity for quality stocks in mid-2011, as the major policy overhang should be largely in the price.

Long-term growth drivers intact — robust market demand growth, policy-driven market consolidation and industry upgrade.

Re-entry opportunities in picking up long-term winners — focusing on long-term beneficiaries of two re-rating themes: market consolidation, industry upgrade.
# China – policy drivers and risks

## Growth amid consolidation – greater long-term opportunities for domestic leaders

### Growth drivers

- Robust long-term sector growth outlook (>20% profit CAGR in next five years), underpinned by the following drivers, in our view:
  - The drug market will sustain at c. 2x GDP growth to catch up with the standards of other developed countries
  - Policy push: expansion in medical insurance coverage, development of rural healthcare infrastructure, strategic growth industries in 12th Five-Year-Plan
  - Geo-economic drivers: solid GDP growth, urbanization and a large ageing population
  - Market consolidation: higher market concentration, M&A opportunities and industry upgrade

### Consolidation drivers

- Cutting retail price of drugs in the NDRL – average 20% in the first two rounds
- Enforcement of “Anhui Model” for the central tendering of EDL – greater pressure on tender price but scope of influence should be c. 10% of total drug market
- New GMP measures – start-up of medical device GMP in 2011 and upgrade of the drug GMP; higher barrier to entry and capex requirement
- Resumption of provincial-level central procurement of high cost medical device and equipment; short-term pressure on product prices
- Diagnosis Related Group (DRG) – reform of the payment scheme in hospitals
- Stringent control in the clinical use of anti-infective drugs
# China – Sector valuation

## Stock picks

### Stocks under coverage - China

<table>
<thead>
<tr>
<th>Bloomberg code</th>
<th>China Shineway</th>
<th>Lijun International</th>
<th>Sino Biopharma</th>
<th>Sinopharm</th>
<th>United Laboratories</th>
</tr>
</thead>
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<tr>
<td>2877HK</td>
<td>17.50</td>
<td>1.76</td>
<td>2.75</td>
<td>27.50</td>
<td>12.00</td>
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<tr>
<td>2005HK</td>
<td>827</td>
<td>2,455</td>
<td>4,957</td>
<td>690</td>
<td>1,302</td>
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<tr>
<td>1177HK</td>
<td>14,473</td>
<td>4,321</td>
<td>13,631</td>
<td>18,983</td>
<td>15,618</td>
</tr>
<tr>
<td>1099HK</td>
<td>12.00</td>
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<td>1,302</td>
<td>1,302</td>
<td>1,302</td>
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<tr>
<td>3933HK</td>
<td>12.00</td>
<td>1,302</td>
<td>1,302</td>
<td>1,302</td>
<td>1,302</td>
</tr>
</tbody>
</table>

| Price (HK$)* | 17.50 | 1.76 | 2.75 | 27.50 | 12.00 |
| Issued shares* (m) | 827 | 2,455 | 4,957 | 690 | 1,302 |
| Market cap* (HK$m)* | 14,473 | 4,321 | 13,631 | 18,983 | 15,618 |

<table>
<thead>
<tr>
<th>Rating</th>
<th>Buy</th>
<th>Reduce</th>
<th>Buy</th>
<th>Neutral</th>
<th>Neutral</th>
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<tr>
<td>Target price (HK$)</td>
<td>30.30</td>
<td>1.68</td>
<td>3.75</td>
<td>29.00</td>
<td>13.00</td>
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<tr>
<td>Upside / downside(%)</td>
<td>7.3</td>
<td>(5)</td>
<td>5</td>
<td>8</td>
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</table>

### Valuation method

- **21x FY11PE; implied 1x PEG**
- **18x FY11PE; implied 1.1x PEG**
- **30x FY11PE; implied 1.1x PEG**
- **32x FY11PE; implied 1x PEG**
- **SOTP: 1.8x P/BV for cyclical assets; 18x FY11PE for finished drugs**

### Valuation

<table>
<thead>
<tr>
<th>PE (X)</th>
<th>2010</th>
<th>2011E</th>
<th>2012E</th>
<th>2013E</th>
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<td>10.1</td>
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<td>Lijun International</td>
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<td>23.5</td>
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<td>15.4</td>
<td>16.4</td>
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<table>
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<th>Yield (%)</th>
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<th>2012E</th>
<th>2013E</th>
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<tr>
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<td>0.7</td>
<td>0.7</td>
<td>0.9</td>
<td>1.2</td>
</tr>
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<td>United Laboratories</td>
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<td>2.1</td>
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<td>2.8</td>
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<table>
<thead>
<tr>
<th></th>
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<td>China Shineway</td>
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<td>3.3</td>
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<tr>
<td>Lijun International</td>
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<td>Sino Biopharma</td>
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<td>Sinopharm</td>
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<td>United Laboratories</td>
<td>3.1</td>
<td>2.7</td>
<td>2.4</td>
<td>2.2</td>
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</table>

Note: * Only includes H shares for H companies

Pricing as of 25 May, 2011; Ratings and Price Targets are as of the date of the most recently published report (http://www.Nomura.com) rather than the date of this document.

Source: Nomura research, Company data, Bloomberg

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India – Four attractive themes

Out-of-pocket spending dominates Healthcare expenditure

Four attractive themes

- Attractive domestic opportunity
- The US opportunity
- The EM opportunity
- Outsourcing

Indian Pharma:

Growth drivers: Volume 60%,
  New Introduction – 40%
- Increased disposable income
- Lifestyle changes
- Increased healthcare infrastructure
- Increased distribution
- Greater awareness
- Increased diagnosis

Healthcare spending in India as % of GDP is low

<table>
<thead>
<tr>
<th>Country</th>
<th>Per-capita expenditure on healthcare (PPP US$)</th>
<th>Government spending on healthcare as % of total gov't spending</th>
</tr>
</thead>
<tbody>
<tr>
<td>Physical</td>
<td>7.6</td>
<td>7.6</td>
</tr>
<tr>
<td>Mental Health</td>
<td>0.9</td>
<td>0.9</td>
</tr>
<tr>
<td>Total</td>
<td>8.5</td>
<td>8.5</td>
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</table>

Scope for expansion in healthcare spending in India

<table>
<thead>
<tr>
<th>Country</th>
<th>Per-capita expenditure on healthcare (PPP US$)</th>
<th>Government spending as % of total spending</th>
</tr>
</thead>
<tbody>
<tr>
<td>India</td>
<td>49</td>
<td>1.2</td>
</tr>
<tr>
<td>World average</td>
<td>650</td>
<td>11.1</td>
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</tbody>
</table>

Healthcare expenditure as % of GDP

<table>
<thead>
<tr>
<th>Country</th>
<th>Government spending as % of total spending</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>15.2</td>
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<tr>
<td>Switzerland</td>
<td>11.4</td>
</tr>
<tr>
<td>Canada</td>
<td>9.7</td>
</tr>
<tr>
<td>France</td>
<td>11.2</td>
</tr>
<tr>
<td>Netherlands</td>
<td>9.2</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>8.2</td>
</tr>
<tr>
<td>Japan</td>
<td>8.2</td>
</tr>
<tr>
<td>Spain</td>
<td>8.2</td>
</tr>
<tr>
<td>Israel</td>
<td>7.8</td>
</tr>
<tr>
<td>Portugal</td>
<td>7.8</td>
</tr>
<tr>
<td>Argentina</td>
<td>7.8</td>
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<tr>
<td>Hungary</td>
<td>7.8</td>
</tr>
<tr>
<td>Republic of Korea</td>
<td>7.8</td>
</tr>
<tr>
<td>Poland</td>
<td>6.2</td>
</tr>
<tr>
<td>South Africa</td>
<td>6.2</td>
</tr>
<tr>
<td>Brazil</td>
<td>7.8</td>
</tr>
<tr>
<td>Mexico</td>
<td>6.4</td>
</tr>
<tr>
<td>Turkey</td>
<td>5.7</td>
</tr>
<tr>
<td>Russian Federation</td>
<td>5.2</td>
</tr>
<tr>
<td>Romania</td>
<td>5.5</td>
</tr>
<tr>
<td>Venezuela</td>
<td>4.7</td>
</tr>
<tr>
<td>China</td>
<td>4.7</td>
</tr>
<tr>
<td>Egypt</td>
<td>6.1</td>
</tr>
<tr>
<td>India</td>
<td>1.0</td>
</tr>
</tbody>
</table>

Source: World Health Organization (WHO), Nomura research
India - Emerging markets- Partnership is the way to go

Surge in opportunities over the next three years

Emerging markets – offer high growth potential, but companies face significant hurdles
- Generic market size estimated at US$52bn, with an estimated CAGR of 12% over the next five years (source: Sandoz)
- Key markets include Russia & CIS, Brazil, South Africa, the Middle East and Romania
- Significant entry barriers owing to the dominant branded generic model – Traditionally, Indian companies resorted to acquisitions to gain a foothold

Japan – an underpenetrated generic market
- Second-largest pharma market globally, but generic penetration is low – 17% by volume, 5% by value
- Government reforms favour generics – targeting 30% volume penetration over the next five years
- Some Indian companies, including Ranbaxy, Zydus Cadila and Lupin, have made forays into this market
- So far, Indian companies have witnessed steady revenue growth – can potentially accelerate in future, in our view

Success has been limited to a few geographies (eg, Russia for Dr. Reddy’s, Brazil and South Africa for Ranbaxy)
- Difficult to profitably manage thin spread across different markets
- High currency fluctuations and debtor-days in the recent past add to the woes

Tie-ups with big pharma – a good way to realise the potential (GSK – DRRD, Torrent – AZN, Aurobindo – PFE, Cadila – ABT).

Panel discussion

Accelerated growth in India Pharma market

Market Opportunities

<table>
<thead>
<tr>
<th>IPM incremental Sales (INRbn)</th>
<th>MAT June 2007</th>
<th>MAT June 2008</th>
<th>MAT June 2009</th>
<th>MAT June 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>35</td>
<td>40</td>
<td>48</td>
<td>72</td>
</tr>
</tbody>
</table>

IPM incremental Sales (INRbn)
Indian companies have consistently gained market share in the US

USFDA has a backlog of ~2,000 ANDAs pending approval; of these, Indian companies account for ~30% by volume.

- Market share for Indian companies ramped up to 18.2% in March 2011, a threefold increase over the past three years. Incremental prescription share of Indian companies was 35.7% as of MAT March 2011.

Pharmaceutical contract manufacturing is estimated at US$35-40bn, approximately 25-30% of pharmaceutical manufacturing

- API/intermediates account for 70% and the rest is formulation. 50% of API/intermediate and 15% of formulation is outsourced.

- Within formulation, it is mostly orals compared to injectables. Indian manufacturers account for approximately US$1bn in sales, just a 2% market share.

- Indian companies primarily focus on API/intermediates. Jubilant is the exception with large presence in injectables.

Pharmaceutical R&D outsourcing is estimated at US$20-25bn, ~25% of pharmaceutical R&D spending

- 70% of the outsourcing is in clinical trials.

- Out sourcing to India can save 60% of costs. Indian companies account for less than US$500mn in revenues, less than a 2% market share.

- Indian companies gaining traction as they move from FTE- and fee-based model to collaborative model.
India – Our top picks

Recommendations

Dr Reddy’s - Buy: A play on US generic opportunity; expectations are still low

Lupin - Buy: Growth likely to accelerate in FY13 on US pipeline; also supported by strong domestic business

Glenmark - Buy: Cheapest front-line generic company; expect improvement in balance sheet and cash flow; no major value attributed to R&D pipeline

<table>
<thead>
<tr>
<th>Company</th>
<th>Ticker</th>
<th>Recommendation</th>
<th>Market cap (US$ bn)</th>
<th>Base business valuation (A)</th>
<th>Others (B)</th>
<th>Target price (=A+B)</th>
<th>CMP</th>
<th>% upside</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sun Pharma</td>
<td>SUNP IN</td>
<td>NEUTRAL</td>
<td>9.4</td>
<td>485</td>
<td>5</td>
<td>490</td>
<td>430</td>
<td>14%</td>
</tr>
<tr>
<td>Cipla</td>
<td>CIPLA IN</td>
<td>NEUTRAL</td>
<td>5.2</td>
<td>316</td>
<td>-</td>
<td>316</td>
<td>305</td>
<td>4%</td>
</tr>
<tr>
<td>Ranbaxy</td>
<td>RRXY IN</td>
<td>REDUCE</td>
<td>4.3</td>
<td>360</td>
<td>102</td>
<td>462</td>
<td>478</td>
<td>-3%</td>
</tr>
<tr>
<td>Dr. Reddy’s</td>
<td>DRRD IN</td>
<td>BUY</td>
<td>5.7</td>
<td>1,949</td>
<td>135</td>
<td>2,084</td>
<td>1,598</td>
<td>30%</td>
</tr>
<tr>
<td>GlaxoSmithKline</td>
<td>GLXO IN</td>
<td>NEUTRAL</td>
<td>4.2</td>
<td>2,479</td>
<td>-</td>
<td>2,479</td>
<td>2,334</td>
<td>6%</td>
</tr>
<tr>
<td>Lupin</td>
<td>LPC IN</td>
<td>BUY</td>
<td>4.0</td>
<td>570</td>
<td>-</td>
<td>570</td>
<td>421</td>
<td>36%</td>
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<tr>
<td>Glenmark</td>
<td>GNP IN</td>
<td>BUY</td>
<td>1.5</td>
<td>367</td>
<td>34</td>
<td>431</td>
<td>270</td>
<td>60%</td>
</tr>
<tr>
<td>Cadila Healthcare</td>
<td>CDH IN</td>
<td>BUY</td>
<td>4.0</td>
<td>937</td>
<td>-</td>
<td>937</td>
<td>910</td>
<td>3%</td>
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</tbody>
</table>
Valuation Methodologies and Risks

Ansell: We use a blend of three valuation methodologies to derive our A$14.67 valuation for ANN: discounted cashflow analysis (DCF), a capitalisation of EV/EBITDA and normalised P/E multiples. We believe this approach is appropriate for ANN because it has a number of listed competitors. As a result, each division’s relative value in the market can be readily ascertained. We use a P/E valuation, as it is a market standard, and an EV/EBITDA valuation metric, as this is frequently used in the global healthcare sector. Upside risks include higher-than-expected volume growth driven by restocking and an increase in industrial production activity; an announcement of an earnings-accretive acquisition or a share buyback. Downside risks include pressure on costs from rising prices of raw material inputs and a slowdown in the global economic recovery.

Cadila Healthcare: Our 12-month target price of INR937 is based on 20x blended FY12-13F EPS. Our valuation multiple is in line with the current trading multiple, but at a 15% discount to front-line generic peers. We believe with improvement in growth visibility, the discount to front-line peers could narrow, presenting further upside to our current target price. We are quite comfortable with the valuation multiple given forecast compound growth of >20% in profits and RoE at 28-30% over the next three years. Risks that could impede the achievement of our price target include but are not restricted to the following: Lower-than-expected growth in emerging market revenues; Significant delay in approval of new products from the US FDA and other regulatory issues; Material delays in execution in the US market leading to delayed launches; Greater-than-expected price decline in any of the markets due to competition or regulatory changes; Lower-than-estimated growth in the Hospira JV and Significant appreciation in the INR against export currencies.

China Shineway: We apply a rolling 12-month forward P/E and PEG method to value the pharmaceutical stocks we cover to reflect 12-month earnings forecasts and long-term growth visibility in the fast-growing healthcare market in China. We derive a target P/E of 21x, in line with the average valuation benchmark of 20x P/E or 1x PEG for leading pharmaceutical stocks. Applied to our FY11-12F EPS forecasts of CNY1.15 and CNY1.46 (implied PEG of 1x), we derive a TP of HKD30.30. Higher-than-expected cut in drug prices, stronger-than-expected raw herb price hike, unfavourable newsflow about TCM injection safety issues and delay in the completion of new capacity expansion.

Cipla: We maintain that Cipla should trade at a discount to front-line generic peers. This is due to relatively poor visibility of export growth and low return ratios. We maintain fair valuation multiple at a 20-25% discount to front-line peers. Hence, we value Cipla at 18x FY13E. We arrive at our 12m target price of INR 316. We maintain Neutral. Upside Risks• Stronger-than-expected growth in domestic formulations• Faster approval and ramp-up in export formulations• Strategic tie-up that presents greater visibility of export ramp-up• Higher technology income• Product-specific upside related to patent expiry—for instance, API or formulation supply to first-to-file partner during exclusivity. Downside Risks• Weaker growth in domestic formulations• Delay in regulatory approvals for export markets• Provision or outgo related to NPPA (National Pharmaceutical Pricing Authority) notice. Cipla has an outstanding notice for INR 12bn. This is related to alleged overcharging for price controlled drugs.

Clinuvel Pharmaceuticals: On a DCF analysis, we derive a price target for CUV, assuming a WACC of 14.25%. We factor in an initial selling price of €1,500 per implant and assume that this will decline by 2% pa. In line with most pharmaceutical companies, we expect CUV to achieve a steady-state gross profit margin of 70%. We believe that any delay or failure to progress in clinical trials would present downside risk to our price target. That said, faster-than-expected progression to production of CUV’s photoprotective technology could provide an upside boost.

Cochlear: We use a blend of three valuation methodologies to derive a valuation for Cochlear: 1) discounted cashflow (DCF) analysis; 2) capitalisation of EV/EBITDA, and; 3) normalised P/E multiples. Our valuation for Cochlear is A$88.00. Upside risks include faster-than-expected growth in Cochlear and BAHA sales. Downside risks include faster-than-expected new product launches from its competitors SOON and Med-EI.

CSL: We use a blend of three valuation methodologies to derive a valuation for CSL: discounted cashflow analysis (DCF), a capitalisation of EV/EBITDA and normalised P/E multiples. We use a P/E valuation as it is a market standard and an EV/EBITDA valuation metric as this is frequently used in the global healthcare sector. Downside risks to our price target include irrational industry behaviour leading to potential oversupply of IG, which, in turn, could lead to price weakness and lower-than-expected HPV revenues from Merck. Upside risks could come from demand for IG to treat Alzheimer’s disease.
Dr Reddy’s Laboratories: We value the base business at 23x one-year-forward earnings, in line with the current sector valuation, to arrive at INR1,949/share. We add value of INR135/share for one-off opportunities. This gives us a target price of INR2,084. Key investment risks are failure to obtain key approvals in the US, negative regulatory changes in key markets, rupee appreciation and a substantial increase in high-risk innovation investments.

GlaxoSmithKline Pharmaceuticals: We value the stock at 27.5x December FY12F EPS (in line with current multiples) and roll forward by two months at 11% cost of equity to arrive at a 12-month PT of INR2,479. Key downside risk: adverse price control regulation. Key upside risks: value-accretive acquisitions, greater-than-anticipated success of new launches.

Glenmark Pharmaceuticals: We expect GNP to trade at a premium to the one-year average P/E multiple of 16x, given its improved debt and receivables position. Based on this methodology, we arrive at a price target of Rs431. We value the core business at Rs397/share (based on 18x FY12-13 blended); R&D at Rs21/share and the Zetia opportunity at Rs13/share. Further, the US could present upside to our assumptions. We are not valuing the R&D pipeline on a product-by-product basis. Risks to our price target include: 1) further deterioration in the working capital cycle of the company; 2) negative developments on the two key advanced molecules in the innovation R&D pipeline; 3) a lower-than-expected revival in emerging market revenues; and 4) a significant delay in the approval of new products by the USFDA.

iSOFT Group: Our A$0.17 target price is based on CSC’s offer price. Risks to the achievement of our target price include staff risks, the potential for earnings volatility, reputation risk and acquisition risk.

Lijun Int’l: We apply a rolling 12-month forward P/E and PEG method to value the pharmaceutical stocks we cover to reflect 12-month earnings forecasts and long-term growth visibility in the fast-growing healthcare market in China. Given Lijun’s lower near-term earnings visibility, we derive a target P/E of 18x, which is at a 10% discount to the average valuation benchmark of 20x P/E or 1x PEG for leading pharmaceutical stocks. Applied to our FY11-12 EPS forecasts of HKD0.088 and of HKD0.105, we derive a TP of HKD1.68. Risks to our investment view mainly come from the possibility that Lijun could become an acquisition or merger target for a larger market leader in the IV infusion market in China.

Lupin: We value LPC at 23x one-year-forward earnings to arrive at a target price of INR 570. The valuation multiple is in line with that of other front-line generic companies. The key risks to our view are a slowdown or fall in branded generic revenues; Suprax and Antara are likely to face generic competition over the next four to five years and need to be replaced over time; appreciation in INR against export currencies; and regulatory changes, including price control in key markets such as India and Japan.

Mesoblast: Using DCF analysis, we value MSB at A$10.45 per share, using a WACC of 16.05%. Our assumptions include: 1) Equity beta — due to its inherent risks, MSB will have a higher beta than most other industrial companies. We assume that the company’s equity (and asset) beta is 1.80, in line with the average beta for higher-risk biotech opportunities.; 2) Nominal long-run growth rate — given the potentially high growth rate of this business, and in line with those of other high-growth companies in the market, we assume a nominal long-run growth rate of 5% and a real long-run growth rate of 2.5%. There is still a good deal of uncertainty around MSB’s viability in most of its prospective markets. Pre-clinical trials, although positive, give no firm indication of a product’s true viability and full foresight on future market conditions is difficult to obtain. Therefore, we believe this is an attractive investment opportunity for investors with a higher risk appetite.

Primary Health Care: We use a blend of three methodologies to derive a valuation for Primary Health Care: 1) DCF analysis, 2) a capitalisation of EV/EBITDA, and 3) normalised P/E multiples. We believe this approach is appropriate for Primary Health Care because it has a number of listed competitors. We use a P/E valuation as it is a market standard and an EV/EBITDA valuation metric as this is frequently used in the global healthcare sector. Our target price for Primary Health Care is A$3.61. Upside risks to our target price include: 1) greater-than-expected synergy from the Symbion Health acquisition; and 2) reimbursement increases from public insurers in Australia. Downside risks: 1) competition issues continuing in the Australian DI industry, and 2) a strong competitive response in Primary Health Care’s pathology markets.

Ramsay Health Care: We use a blend of three valuation methodologies to derive a valuation for RHC. These are discounted cashflow analysis (DCF), a capitalisation of EV/EBITDA, and normalised P/E multiples. We believe this approach is appropriate for RHC because it has a number of listed competitors. As a result, each division’s relative value in the market can be readily ascertained. We use a P/E valuation as it is a market standard and an EV/EBITDA valuation metric as this is frequently used in the global healthcare sector. Currently, we factor in no future acquisitions when developing our valuation for RHC, and our blended valuation and target price of A$18.35 for RHC are unchanged. Upside risks to our target price include greater-than-expected revenue growth of the hospitals division owing to higher reimbursement from private health insurers. Downside risks include margin compression, particularly in the Australian pathology business.
Panel discussion

**Ranbaxy:** We use DCF to value Ranbaxy’s base business at INR360/share as we think metrics such as P/E or EV/EBITDA cannot be used for RBXY’s unsteady business in the near term. The key assumption of our DCF model is a 15% medium-term growth rate between 2012F and 2017F and 6% terminal growth rate thereafter. We assume the EBITDA margin will rise to 15% in 2016F from 7.2% in 2011. We use cost of equity of 12%. Over the long term we are factoring in Net Debt/Equity of 0.7 and RoE of 25%. Incorporating the one-time value at INR102/sh, we arrive at a price target of INR462/sh, representing downside potential of 22% from the current level. Upside risks to our price target include, but are not restricted to: higher-than-expected sales and margins from exclusive product launches such as Lipitor, Aricept, Nexium, etc; stronger-than-expected sales performance in India and other emerging markets; and favourable currency movements leading to higher financial income.

**ResMed:** We use a blend of three valuation methodologies to derive our A$4.32 valuation for RMD: these are discounted cashflow analysis (DCF), a capitalisation of EV/EBITDA (based on 13.7x FY12 EBITDA) and normalised P/E multiples (based on 23.1x FY12 EPS). Upside risks to our target price include a faster-than-expected rollout of home diagnosis testing in the US market. On the downside, there is a risk that another competitor could significantly decrease prices for its CPAP machines and masks/appliances to gain market share.

**Sino Biopharmaceutical:** We apply a rolling 12-month forward P/E and PEG method to value the pharmaceutical stocks we cover to reflect 12-month earnings forecasts and long-term growth visibility in the fast-growing healthcare market in China. Our TP of HKD3.75 is based on 30x 12-month rolling P/E and FY11-12F EPS of HKD0.114 and HKD0.155, which is at a premium to the average valuation benchmark of 20x P/E or 1x PEG for leading pharmaceutical stocks, reflecting the strong long-term growth visibility amid central policy support for its M&A expansion strategy. Downside risk to our NEUTRAL call: potentially lower-than-expected IPO P/E for SHP. Upside risk: greater-than-expected policy benefits from the 12th FYP.

**Sonic Healthcare:** We use a blend of three valuation methodologies to derive our target price for Sonic Healthcare: discounted cash flow analysis (DCF), a capitalisation of EV/EBITDA and normalised P/E multiples. We believe this approach is appropriate for Sonic Healthcare because it has a number of listed competitors. We use a P/E valuation as it is a market standard and an EV/EBITDA valuation metric as this is frequently used in the global healthcare sector. Our target price for Sonic Healthcare is A$11.91. Downside risks to our price target: 1) if the expected increase in revenue from the EU pathology business fails to materialise; and 2) margin compression in the Australian pathology and DI businesses. Upside risks include another accretive acquisition.

**Sun Pharmaceutical Industries:** We value Sun Pharma at 23x one-year forward earnings, in line with the other front-line generic companies, to arrive at our base-business price target of Rs485. We expect Sun Pharma to trade at 20-25x one-year forward earnings. While one may argue for a higher multiple for a stronger domestic business, we believe this will be negated by: 1) a lower return ratio due to unutilised cash; 2) a very low tax rate, which can rise substantially in future; and 3) lower-than-peers R&D spending on innovation R&D is housed under a separate company SPARC and to that extent, profits are overstated. Given that upsides from Protonix and Eloxatin are already largely factored into its cash flow, the only material product opportunity (that is not sustainable in nature) is the six-month exclusivity for Imatinib, in our view. We value this opportunity at Rs5/sh.

**United Laboratories:** We apply the SOTP method to value United Laboratories to capture the different earnings performance features of its two different segments: 1) the commodity-like API segment; and 2) the finished drugs segment. Our TP of HKD13.0 is based on 1.8x P/BV (HKD7.87 on NAV of HKD4.37) for the intermediate and bulk pharmaceutical segments, which is based on its ROE of 18%. We value the finished drugs segment at 18x forward P/E (FY11F EPS of HKD0.28 from finished drugs), which is in line with the benchmark average for leading generic drug makers. This results in our HK$13.0 target price. Upside risks: India’s anti-dumping tariff proposal may be rejected in a later stage; competition from newly built 6-APA capacity may come later than our expectations; faster-than-expected growth in the market from new insulin products. Downside risks: Worse-than-expected adverse impact from newly built capacity and India’s anti-dumping tariff to intensify over-capacity problems in China’s 6-APA market.
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As at 31 March 2011.

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Explanation of Nomura's equity research rating system for Asian companies under coverage ex Japan published prior to 30 October 2008

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A ‘Neutral’ recommendation indicates that upside or downside is less than 10%.
A ‘Reduce’ recommendation indicates that downside is between 10% and 20%.
A ‘Sell’ recommendation indicates that downside is more than 20%.

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Panel discussion

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