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INDIA

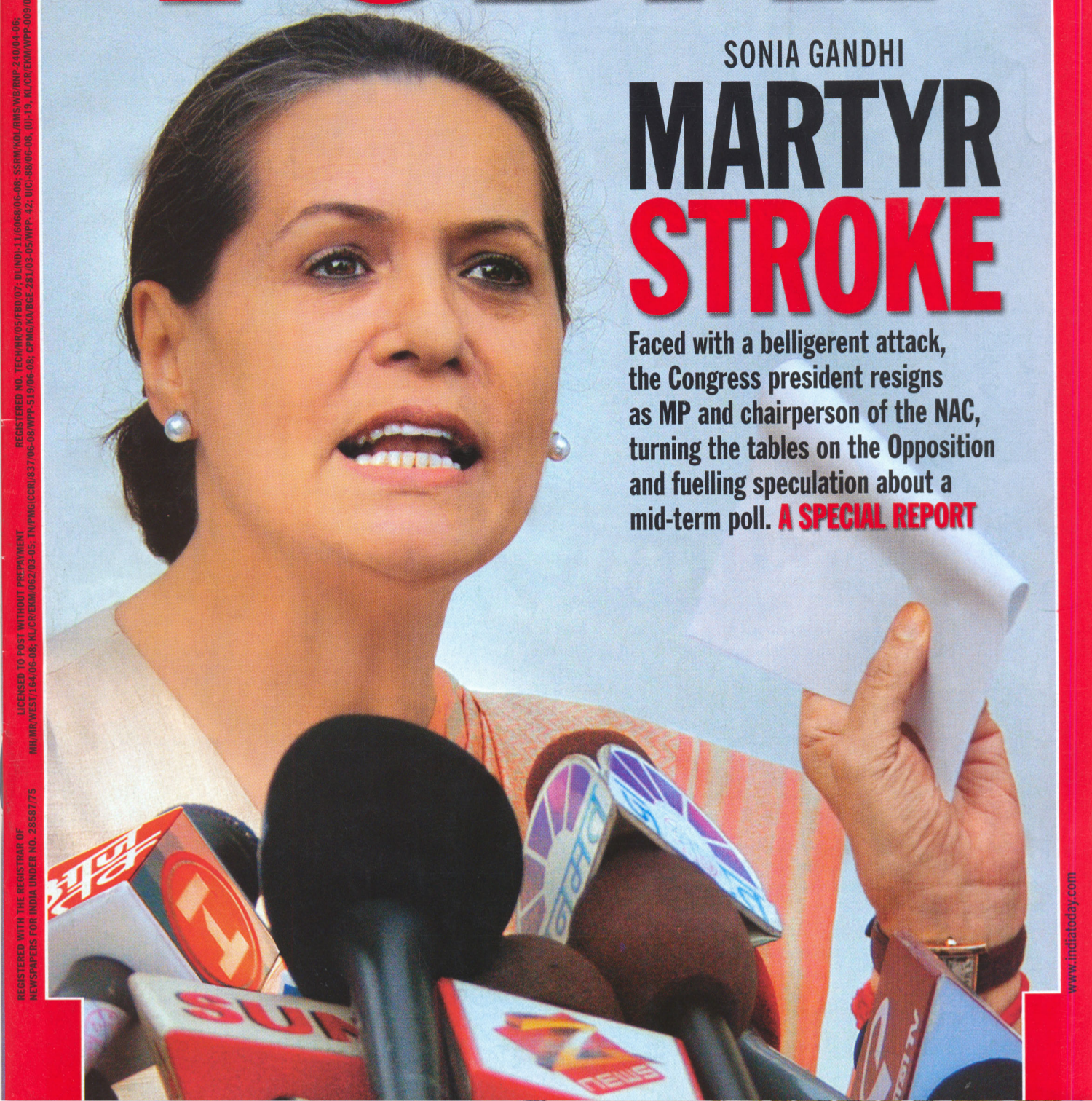
APRIL 3, 2006

TODAY

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STROKE

Faced with a belligerent attack, the Congress president resigns as MP and chairperson of the NAC, turning the tables on the Opposition and fuelling speculation about a mid-term poll. **A SPECIAL REPORT**


business&economy DRL TAKEOVER

PRESCRIPTION FOR SUCCESS

With the Rs 2,500 crore takeover of a top German pharma firm, Dr Reddy's Laboratories not only ensures a strategic global presence, but also enters the top-three league on home ground

By Amarnath Menon

Once bitten, twice shy. Dr. Kallam Anji Reddy certainly does not believe in that axiom. Exactly two years after he failed to buy the German generic drug maker betapharm Arzneimittel GmbH, the founder chairman of Dr Reddy's Laboratories (DRL) finally has it in his bag. Hailed as the biggest ever acquisition by an Indian pharma firm (and the largest European buy-out), the Rs 2,500 crore all-cash

transaction has catapulted DRL into the top five league in the European Union's generics market, and the top three on home ground. Generic drugs are those that are not protected by patents hence companies like DRL can mass produce them at low costs. It is also, possibly, India's first online overseas takeover deal. The icing on the cake? Reddy finally got to even the score with 3i, the European private equity and venture capital company that had won the bid for betapharm in March 2004.

DRL refused to leave anything to

EYE ON THE GLOBAL PIE: Dr K. Anji Reddy is ready to take on the world chance this time round, especially with heavyweights like Ranbaxy, India's No. 1 pharmaceutical company, also in the race. Reddy put together a 20-strong team led by executive vice-president V.S. Vasudevan to present DRL's case and make its offer. "We put up a structured way for completing the process instead of being tentative and indulging in endless negotiations, something most Indian firms have a reputation for, especially when striking large deals," says Vasudevan.

That, along with DRL's debt-free balance sheet, probably tipped the scales in the Hyderabad-based company's favour. By February 10, DRL's CEO, G.V. Prasad, was flying down to Munich to sort out residual issues and clearances with Bernie Schuler of 3i's European buyout business at the office of betapharm's lawyers Clifford Chance. On February 16, the two sides, comfortably ensconced in their offices in Munich and Hyderabad, inked the 30-page share purchase agreement over the Internet in true German tradition wherein every clause of the


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THE BIG DEAL

WHAT This is the biggest ever acquisition deal by an Indian pharma company. The German major, betapharma, cost DRL a whopping Rs 2,500 crore.

WHY The takeover gives DRL a strategic presence in Europe. Significantly, the company will no longer be as dependant on the US market, which has not been faring well in the last 18 months and the forecasts aren't any better.

WHERE The acquisition will take DRL among the top 10 in Europe, the world's second largest generics market. It rejigs the order at home too. Though no one wants to say how will DRL move up the pecking order, it will certainly move into the top-three league.

HOW Once the patent regime in Europe expires, DRL would be in a position to cash in on generic drugs opportunities worth \$14.2 billion in the continent's largest markets—UK, France, Italy and Germany.

agreement is read out before pens are drawn and champagne bottles are popped.

"Betapharm has what DRL needs and more. The company is the fastest growing with a drug pipeline that should see it emerge on the top, over the next few years," exults Prasad. Based in Augsburg, betapharm is Germany's fourth-largest generic pharmaceuticals company with a 3.5 per cent market share and revenues of Euro 165 million (Rs 863 crore) in 2005. The company may not have its own manufacturing facility but it gives DRL access to a wide range of products dominated by drugs to treat heart ailments apart from those of the nervous system. To capitalise on its brand equity, DRL will retain the betapharm name as well as all 370 employees. As part of the deal, DRL will also be taking over the Beta institute, a non-profit organisation set up by the company for medical education and patient follow up.

So what does DRL gain from this deal? "The immediate gain is an addition of \$200 million (Rs 887 crore) to our revenue but, in the long term the acquisition will enable us have a stronger presence in Europe," says Prasad (see box). Analysts predict that DRL can also leverage on this acquisition as the four largest markets in Europe—UK, France, Italy and Germany—are set to witness patent expirations from this year itself opening up opportunities of around \$14.2 billion (Rs 631.4 billion). According to Merrill Lynch estimates, assuming a 60 per cent fall in prices post patent expiry and an as much volume penetration, this would create a \$5.1 billion (Rs 226.8 billion) generic opportunity. If a company can garner even a 10 per cent market share, it will result in sales of around \$510 million (Rs 2,250 crore).

HARD DRIVE AHEAD: DRL hopes to become a discovery-led global pharma major in the near future

Another significant advantage of the acquisition is that DRL will no longer be as dependent on the US market as it has been in the past. Since the American market has not been doing well, all Indian pharma companies have suffered over the last 18 months. Ranbaxy has said at successive quarterly results announcements that US is pulling it down and forecasts aren't getting any better. With this coup, DRL has successfully managed to diversify beyond the US.

As MNCs strengthen their presence in the local market to beat the margin and revenue pressures in the US—the largest and easiest market to enter so far—Indian drug makers are increasingly responding by way of overseas acquisitions, particularly in Europe and Japan. This is one such major strategic buy attempted by a desi pharma company to get a head start in market share abroad, especially the world's second biggest generic market. In fact, DRL post the acquisition stands at the number four slot, right behind global majors like Sandoz, Rationpharm and Stada.

However, post the takeover euphoria, tongues are beginning to wag about the winner's curse phenomena, that is when the top-bidder overshoots his budget. Some analysts now argue that the acquisition price was somewhat high given that the enterprise value is nearly three times betapharm's revenue last year. The deal has also stretched DRL's financials to the maximum. The buy out price, the highest doled out by an Indian company for an overseas acquisition, was 39 times DRL's profit in 2004-05 and larger

than its revenues of \$446 million (Rs 1,980 crore). Also, DRL ended up paying \$214.5 million (Rs 952 crore) more compared to what 3i shelled out for betapharm two years ago. But Reddy contends, "We are happy with the price because this is a strategic buy," adding, "The spirit of the price is essential to compete with the best in the world."

DRL is doing exactly that. This is the company's second acquisition in Europe. In 2002, it acquired the UK-based BMS Laboratories and its wholly owned subsidiary, Aurigene Discovery Technologies, for about \$12 million (Rs 53 crore). In November last year, DRL bagged Roche's API business, in Cuernavaca, Mexico, in a \$59 million (Rs 262 crore) deal. "With the betapharm acquisition we will make good profits this year. That is important to exist and grow on the stock market," says Reddy.

While such takeovers will help establish a strong presence in the fast growing global generics market, Reddy is relying heavily on what the Dr Reddy's Research Foundation is expected to deliver in the next two years. "We are making the transition from being copycats to innovators," he says. DRL's research scientists are working hard to discover new drugs. They have had few early breaks but the new drugs are yet to make the grade. However, Reddy is upbeat about being on the right track. "We have laid our roadmap with a penchant for innovation and the ability to take a discovery-led global pharma company soon. Moving towards that goal, DRL has already perfected the balance between making profits today and investing in future growth." **with Puja Mehra**