Erste Sector Healthcare

CEE Pharma 2010 outlook - 3 February 2010

CEE pharma stocks offer interesting long-term upside potential, short-run performance dictated by swings in risk appetite

Improving macro picture, stabilizing Russia bode well for Hungarian pharmas, R&D progress set to add more shine to Richter valuation

Krka's long-term regional competitive edge should warrant stock's appreciation from currently depressed levels

Bioton's restructuring (and Polpharma cooperation) promises to unlock its potential

Romanian pharmas to cope with regulatory pressures, privatization prospects to brighten long-term horizon

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Executive summary

CEE pharma stocks underperformed their respective markets in 4Q09, reflecting the increasing risk appetite of investors who turned their attention towards cyclical stocks. Nonetheless, for the full year, the CEE pharma sector companies still ended (with the exception of restructuring-plagued Bioton) in black territory, with high double-digit-term y/y performances mostly ahead of the local indices. Also in 2010, CEE pharma stocks, representing a safe haven in times of turbulences and uncertainty, will undoubtedly continue to be driven by (apart from their business results) changing investor sentiment. However, with their current valuations far below their earlier peaks, the top CEE pharma stocks retain their long-term appeal.

While wrapping up 2009, for the upcoming reporting season, CEE pharma companies are expected to provide first guidance for 2010. We believe that the top CEE pharma companies are poised to deliver solid business results, although - due to the restrictive drug pricing / reimbursement measures - the tempo might be somewhat tempered compared to pre-crisis days. Importantly, in Russia/CIS, the situation continues to stabilize. Bolstered by the appreciating ruble, as well as the recovery of oil prices, the crucial Russian market is getting back on track, playing in favor of the performance of CEE-based pharmas.

We reviewed our models and set new 12-month target prices for CEE pharma stocks. Unlike in 2009, heavily export-geared Hungarian pharmas cannot rely on the supportive effect from the y/y weaker forint in 2010. On the other hand, with the HUF heading for stabilization, the quarterly volatility of their financial results should diminish and the improving Hungarian macroeconomic picture (reflected in decreasing government bond yields) should bode well for the Hungarian pharmas' valuations. The (at least partial) closing of the valuation gap should propel Egis' share price appreciation, while for Richter the R&D pipeline progress should provide a desirable stock trigger. In summary, our target prices for Richter and Egis arrive at HUF 48,200 per share and HUF 21,755 per share, respectively, up 5% and down 4% compared to our previous targets. We hence stick to our Accumulate recommendations for both companies.

Krka's top line tempo was subdued in 2009 and is seen to slow down to single-digit terms in 2010. Nonetheless, even without a currency cushion (enjoyed by its Hungarian peers), Krka's profitability margins continued to beat its regional rivals' in the course of 2009 and the company is poised to witness a stable business performance, with profitability parameters fueled by its strong innovation drive, also going forward. While the share price recovery still might take some time, the currently depressed price levels remain very inviting. With a revised target price of EUR 92.0 per share, we confirm our Buy recommendation.

While Bioton's 2009 results are anticipated to stay deeply in red territory, the outlook for 2010 is not as gloomy, should the company's restructuring plans (in particular, the disposal of certain assets and cooperation/merger with Polpharma) materialize. The news flow related to the restructuring promise remains the main catalyst for the recently ailing share price. As before, we opt to remain on the conservative side and stick to our Hold recommendation. Adjusting our model to incorporate the worse than expected 2009 interim results, delays in timing of the Bioton Wostok disposal and insulin market launch in China, as well as the newly introduced risk-related discount, yields a new 12-month target price of PLN 0.21 per share (vs. the earlier PLN 0.26).

Although Romanian pharmas' forex fortunes are set to be slightly more favorable this year, we expect their profitability margins to be squeezed by the worsening payment discipline and sales tax recently introduced in Romania. We revise our Antibiotice target price to RON 0.624 per share and confirm our Reduce recommendation on the stock. Although we continue to view Biofarm's position as slightly better, not least due to the company's lower exposure to the currently troubled reimbursed drug segment, our revised target price of RON 0.222 points to limited upside potential at the moment and we stick to Hold.

Valuation Summary

Company	Rep. Curr.	Mcap (EURmn)	Price Current (LC)	Target	Recommendation	Performance (EUR terms) 1M	3M	6M	12M
A&D Pharma	EUR	116.7	3.5	3.7	Accumulate	-12.5%	-7.9%	45.8%	75.0%
Antibiotice	RON	71.9	0.645	0.624	Reduce	2.4%	-3.0%	-6.5%	78.7%
Biofarm	RON	56.6	0.211	0.222	Hold	5.0%	5.5%	3.4%	224.6%
Bioton	PLN	265.2	0.20	0.21	Hold	-13.0%	-13.0%	-33.3%	0.0%
Egis	HUF	543.3	18,850	21,755	Accumulate	0.2%	-4.8%	-1.2%	61.1%
Intercell	EUR	1,133.6	24.0	33.6	Buy	-7.4%	-8.7%	-6.7%	-6.5%
Krka	EUR	2,329.6	65.8	92.0	Buy	2.7%	-9.5%	-7.1%	21.1%
Richter Gedeon	HUF	2,842.6	41,200	48,200	Accumulate	-4.0%	5.4%	11.5%	55.2%
Sanochemia	EUR	30.0	2.95		Reduce	5.4%	19.0%	51.3%	14.3%
Teva Pharmaceutical	ILS -	37,471	-	-	-	3.5%	18.8%	7.8%	26.2%
Mylan Inc.	USD	3,985	-	-	-	1.5%	18.0%	40.2%	46.4%
Watson Pharmaceuticals	USD	2,933	-	-	-	0.1%	16.0%	12.8%	30.3%
STADA Arzneimittel AG	EUR	1,427	-	-	-	0.2%	33.1%	42.3%	28.9%
Ranbaxy Laboratories	INR -	2,936	-	-	-	-9.9%	24.4%	69.4%	108.2%
Recordati	EUR	1,095	-	-	-	0.7%	-0.7%	11.6%	34.7%
Dr Reddy Laboratories	INR -	3,085	-	-	-	6.8%	26.2%	52.2%	155.8%
EuroStoxx Healthcare		134,959	-	-	-	9.2%	13.5%	17.3%	0.0%

Source: Erste Group Research, Factset, based on closing prices as of February 1, 2010

Valuation

Richter and Krka continue to top our recommendation list, followed by Egis

With the exception of Bioton, the CEE pharma stocks' share price performance remained in positive territory for the full year 2009 and the vast majority of them managed to beat even the strongly advancing respective bourse indices. Nonetheless, after the 1H09 rally, the tempo slowed down significantly, with all CEE pharma stocks (except Richter) recording negative returns in 4Q09. The main reason was the changing market sentiment, with investors lured by cyclicals; sectors that had earlier been severely punished, such as financials and real estate, enjoyed a boom. Consequently, this resulted in underperformance of defensive titles, including regional pharmas.

A brief look at the current valuations demonstrates that, despite the hefty 2009 appreciation, the key CEE pharma players' stocks still offer solid long-term upside potential. The Hungarian currency's y/y weakening in 2009 provided support to the 2009 results for both Hungarian pharmas (with significant shares of export revenues and the majority of costs incurred in HUF), bolstering their top line performance and profitability margins. Although the year 2010 is less favorable from this perspective, the forint is set to see stabilization, boding well for decreasing volatility in their financial results. Furthermore, as demonstrated by 2009 interim developments, the domestic pharmaceutical market of Richter and Egis does not represent a reason for substantial worry and we continue to believe that the market has already bottomed out and should see a return to (albeit low single-digit) growth. The overall more favorable macroeconomic picture is anticipated to result in a further decrease of yields on governments bonds, another factor boding well for Hungarian pharma valuations in 2010. All told, our new target prices (HUF 21,755 per share for Egis and HUF 48,200 per share for Richter) reassure us that Egis and Richter's long-term upside potential has yet to evaporate. We thus leave our Accumulate recommendations for both companies unchanged. Given last year's steeper stock rally of Egis, as well as Richter's long-term strategic edge, to be supported by the upcoming R&D pipeline progress related news flow, we stick to our stronger preference for the latter stock.

The preliminary 2009 data confirmed that unfavorable currency effects coupled with delays in certain product launches put a brake on Krka's top line pace last year. The outlook for 2010 is more optimistic, however. The regional currencies' recovery vs. the euro along with stabilization of Russia/CIS markets should bolster the sales growth. The company's profitability margins are set to remain superior, backed up by the traditionally cost-conscious management approach as well as Krka's innovative generics portfolio. We continue to believe that, given its regional edge, Krka deserves to be traded at a premium to its peers. Reflecting the somewhat lower than earlier envisaged tempo, our revised target price arrives at EUR 92.0 (vs. the earlier target of EUR 103.0) per share, pointing to significant room for appreciation from its recently depressed levels. Consequently, we confirm our Buy recommendation on the stock.

Restructuring news flow still decisive for Bioton share price developments

Incorporating the bigger than anticipated restructuring blow to the 1-3Q09 results, delays in the Bioton Wostok disposal and in the insulin market launch in China, as well as the newly introduced risk related discount, our new 12-month target price for Bioton is PLN 0.21 per share, somewhat below the earlier PLN 0.26. Here we want to emphasize that, given the low visibility of the intended cooperation deal with Polpharma (including disposal of the antibiotics unit and the Italian companies), our forecasts have yet to reflect the impact of the prepared transaction(s). As time passes, the details (to be provided in 2010) might provide a catalyst to the share price (with the deal set to unlock Bioton's business potential). We thus stick to our conservative stance and our Hold recommendation. Although the current restructuring phase means that the stock's multiples are presently the most demanding in the CEE pharma universe, investors should continue to focus on the planned operational revamp, with future share price developments keeping their strong correlation with the related news flow.

The worsening conditions on the Romanian pharmaceutical market, marked by ever-prolonging payment terms, with the state practically not paying for reimbursed drugs since June 2009, prompt a more cautious approach going forward. In addition, although the measures for the law implementation are facing delays, Romanian pharma manufacturers will have to cope with the negative effect from the new sales tax in 2010. All told, we continue to see Antibiotice (with its bigger exposure to the reimbursed drugs segment) as more severely hit and, while we raise our target price to RON 0.624 per share, we stick to our Reduce recommendation on the stock. For Biofarm, with a slightly brighter outlook, due not least to the company's more favorable sales mix (with a higher proportion of OTC drugs), we reiterate our Hold recommendation, with a target price adjusted marginally upwards, from RON 0.21 to RON 0.222 per share.

CEE pharmaceuticals valuation at a glance

	P/E				P/CE				P/BV			
	2008	2009e	2010e	2011e	2008	2009e	2010e	2011e	2008	2009e	2010e	2011e
A&D Pharma	nm	10.5	8.9	7.2	12.0	6.2	5.3	4.4	0.3	0.5	0.5	0.4
Antibiotice	14.1	19.6	17.5	11.3	6.6	10.5	9.3	7.0	0.7	1.2	1.0	0.9
Biofarm	nm	12.7	17.7	13.9	n.m.	10.3	13.2	10.8	0.7	1.6	1.4	1.3
Bioton	nm	nm	11.5	22.0	n.m.	n.m.	8.7	13.3	0.6	0.8	0.7	0.7
Egis	6.5	12.2	10.8	9.2	4.2	7.6	6.8	6.0	0.8	1.2	1.0	0.9
Intercell	57.9	nm	nm	41.1	49.3	n.m.	102.1	33.2	3.0	3.1	3.1	2.9
Krka	11.0	13.3	14.2	12.6	7.3	9.2	9.5	8.5	2.2	2.5	2.2	1.9
Richter Gedeon	12.1	16.7	15.7	13.7	8.1	11.5	10.6	9.4	1.6	2.1	1.9	1.7
Sanochemia	nm	nm	97.0	28.0	64.4	16.4	5.4	4.4	0.9	0.6	0.6	0.6
Median CEE	**12.1**	**13.0**	**15.0**	**13.7**	**8.1**	**10.3**	**9.3**	**8.5**	**0.8**	**1.2**	**1.0**	**0.9**
Teva Pharmaceutical	19.8	17.3	12.5	11.4	16.3	15.6	11.0	9.7	2.9	2.8	2.4	2.0
Mylan Inc.	22.7	14.7	12.0	10.1	15.5	13.6	8.5	5.2	2.3	2.6	1.9	1.3
Watson Pharmaceuticals	18.9	15.4	12.1	12.0	11.5	12.1	9.1	6.5	2.1	1.8	1.7	1.3
STADA Arzneimittel AG	15.5	14.6	12.6	11.7	9.6	8.8	7.7	7.2	1.7	1.6	1.5	1.4
Ranbaxy Laboratories	nm	78.8	33.4	19.0	nm	43.7	22.2	17.7	3.8	4.4	3.7	2.9
Recordati	10.9	9.6	11.6	10.6	8.1	7.5	8.9	8.7	2.4	2.1	2.0	1.8
Dr Reddy Laboratories	nm	25.2	18.1	15.3	28.0	17.1	12.8	13.4	5.0	4.8	3.7	3.1
Median Peer Group	**18.9**	**15.4**	**12.5**	**11.7**	**13.5**	**13.6**	**9.1**	**8.7**	**2.4**	**2.6**	**2.0**	**1.8**
EuroStoxx Healthcare	18.8	17.0	16.3	14.7	13.2	12.1	10.9	10.0	2.4	2.3	2.1	1.9
CEE to Peer, Prem/Disc	**-36%**	**-16%**	**19%**	**17%**	**-40%**	**-24%**	**2%**	**-2%**	**-69%**	**-55%**	**-47%**	**-47%**

	EV/Sales				EV/EBITDA				Dividend yield			
	2008	2009e	2010e	2011e	2008	2009e	2010e	2011e	2008	2009e	2010e	2011e
A&D Pharma	0.2	0.3	0.3	0.3	4.7	4.6	4.2	3.7	0.0%	0.0%	0.0%	0.0%
Antibiotice	0.8	1.7	1.4	1.2	4.5	8.7	9.1	6.5	5.1%	2.6%	2.3%	3.5%
Biofarm	0.7	2.9	2.4	2.0	2.5	10.6	9.5	7.0	0.0%	0.0%	0.0%	0.0%
Bioton	3.4	4.6	2.6	2.7	-21.0	-29.2	7.7	10.7	0.0%	0.0%	0.0%	0.0%
Egis	0.8	1.2	1.1	1.0	4.7	6.7	5.6	4.6	1.0%	0.6%	0.6%	0.6%
Intercell	15.7	14.9	9.2	6.3	-81.1	-46.3	113.1	24.5	0.0%	0.0%	0.0%	0.0%
Krka	2.0	2.6	2.5	2.2	6.2	7.5	7.8	7.0	2.2%	1.7%	1.8%	2.1%
Richter Gedeon	1.8	2.7	2.3	2.0	8.0	10.2	8.8	7.4	2.2%	1.4%	1.6%	1.7%
Sanochemia	1.6	1.0	0.9	0.8	13.4	23.0	6.1	4.6	0.0%	0.0%	0.0%	0.0%
Median CEE	**1.6**	**2.6**	**2.3**	**2.0**	**4.7**	**7.5**	**7.8**	**7.0**	**0.0%**	**0.0%**	**0.0%**	**0.0%**
Teva Pharmaceutical	3.8	4.0	3.4	2.9	13.2	13.0	9.3	8.2	0.8%	1.0%	1.1%	1.3%
Mylan Inc.	1.6	2.1	1.9	1.6	7.8	8.1	7.5	5.9	0.0%	0.0%	0.0%	0.0%
Watson Pharmaceuticals	1.2	2.0	1.4	1.2	5.8	8.0	6.3	5.7	0.0%	0.0%	0.0%	0.0%
STADA Arzneimittel AG	1.3	1.5	1.4	1.4	8.7	9.3	8.5	7.8	2.1%	2.5%	2.8%	3.2%
Ranbaxy Laboratories	1.8	3.3	2.5	2.2	20.5	46.3	16.9	11.4	1.7%	0.3%	1.7%	1.6%
Recordati	1.3	1.5	1.6	1.3	5.1	5.8	6.6	5.9	4.8%	4.8%	4.8%	n.a.
Dr Reddy Laboratories	1.3	2.8	2.4	2.1	7.1	14.0	11.3	9.3	0.5%	0.5%	0.6%	0.6%
Median Peer Group	**1.3**	**2.1**	**1.9**	**1.6**	**7.8**	**9.3**	**8.5**	**7.8**	**0.8%**	**0.5%**	**1.1%**	**1.3%**
EuroStoxx Healthcare	2.2	2.6	2.4	2.3	9.2	10.2	9.2	8.3	1.6%	1.6%	1.8%	2.0%
CEE to Peer, Prem/Disc	**17%**	**25%**	**21%**	**22%**	**-40%**	**-19%**	**-8%**	**-9%**	**-100%**	**-100%**	**-100%**	**-100%**

Source: Erste Group Research, Factset. Based on closing prices as of February 1, 2010. All data in EUR terms.

Market Overview

CEE equity markets rebound…

…but increasing risk appetite hurts defensives, including pharmas

Despite the hefty gains, only a few of the CEE equity markets (namely Hungary, Russia and Turkey) posted 2009 performance that offset the big double-digit slump of 2008. Nonetheless, the increasing risk appetite continued to play in favor of the CEE region and the region's catching up for the lost performance was remarkable in the second half of 2009, with the emerging equity market funds recording money inflows and trading volumes starting to pick up. Unfortunately, for CEE pharma stocks (as for other defensives), the decreasing risk aversion was bad news. Not only did their tempo lag behind those of the banks, real estate titles and cyclicals, in 4Q09 it slipped into negative territory, vastly underperforming the respective market indices. Also going forward, pharma stocks are poised to witness the pros and cons of their defensive nature. For 1Q10, the sentiment is foreseen to favor cyclicals, with investments in pharma titles to be sidelined. However, as economic conditions remain fragile and with a still negative impact of the economic slowdown witnessed in cyclicals' business results, we might see a change in investment style later in the course of the year, with a return of investors to defensive titles. We believe that healthcare - and especially generics players - should then be among the preferred picks.

CEE pharma stocks performance solid last year

	LC terms					EUR terms				
	% Change 1Q09	% Change 2Q09	% Change 3Q09	% Change 4Q09	% Change 2009	% Change 1Q09	% Change 2Q09	% Change 3Q09	% Change 4Q09	% Change 2009
Antibiotice SA	10.0%	81.8%	0.7%	-13.1%	65.8%	4.6%	83.2%	0.5%	-13.4%	66.4%
Biofarm SA	2.7%	128.5%	19.7%	-8.2%	168.3%	-2.4%	130.2%	19.4%	-8.6%	169.3%
BET (RO)	-18.4%	45.1%	28.0%	6.7%	61.7%	-23.2%	46.0%	28.3%	6.5%	53.3%
Bioton S.A.	10.0%	18.2%	0.0%	-11.5%	-8.0%	-3.1%	23.7%	5.4%	-8.7%	-8.7%
WIG 20 Bench (PL)	-15.5%	23.2%	17.7%	9.0%	31.0%	-25.6%	29.0%	24.1%	12.5%	30.0%
Egis Plc	13.7%	53.9%	12.0%	-4.0%	76.3%	-2.0%	74.2%	13.0%	-4.1%	79.8%
Richter Gedeon	-11.1%	37.8%	9.5%	12.6%	33.7%	-23.4%	56.0%	10.4%	12.6%	36.3%
BUX Bench (HU)	-9.6%	34.9%	32.0%	4.9%	66.3%	-22.1%	52.8%	33.1%	4.9%	69.7%
Krka	9.0%	32.9%	3.0%	-11.1%	32.4%	9.0%	32.9%	3.0%	-11.1%	32.4%
SBI Bench (SI)	-3.3%	17.6%	-1.6%	-5.7%	4.3%	-3.3%	17.6%	-1.6%	-5.7%	4.3%

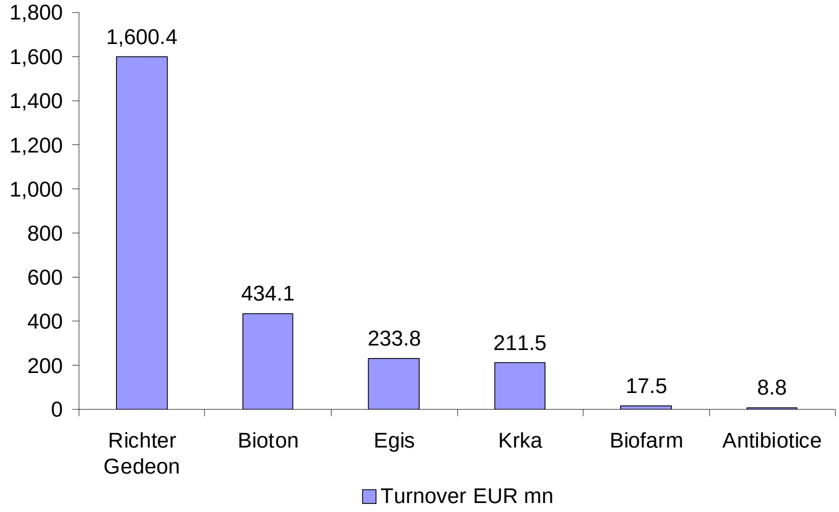
Source: Erste Group Research

CEE pharmas kept outperforming their home markets in 2009, although tempo of appreciation slowed down

Restructuring pains, management changes tempered optimism and put lid on Bioton share

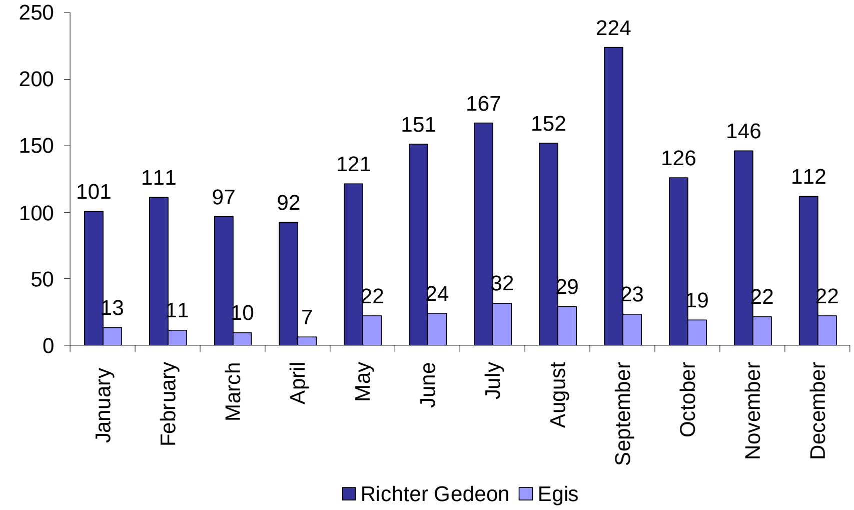
A closer look at the CEE pharma stocks' performance data clearly demonstrates that the swinging market sentiment (which helped to lift share prices of cyclicals, banks and real estate titles) took a relatively heavy toll, erasing part of the earlier gains in 4Q09. Moreover, Hungarian pharma stocks' charts point to another undesirable effect of changing investor risk appetite - their liquidity was shrinking towards the end of the year. Nevertheless, on the cumulative basis, CEE pharmas' stock price performances (except Bioton) for FY09 remained in high double-digit terms. Although the push for Richter and Egis' business results from the weak forint fell in the second half of the year, investors proved to be less sensitive to currency swings than in the past, and the share price performance-forint correlation of Richter and Egis was minimal last year. Moreover, the forint firming not only did not result in a punishment for the stock prices of the Hungarian export-geared pharma companies, but – perceived as confirmation of healthier than thought macroeconomic fundamentals – rather helped to channel more money flows into the Hungarian equity market, with both Richter and Egis benefiting from the developments. In relative terms, Egis outperformed its local rival, enjoying its truly bargain position at the beginning of the last year. While the restructuring story bolstered Bioton's share price performance, it did not shelter the stock completely from the negative impact of sets of bad interim results. The stock was the only one that ended in negative territory last year, slipping by 8.7% in EUR terms in 2009 (vs. a WIG gain of 30%). With its share price climbing by 169.3% in EUR terms, Romania's Biofarm topped the CEE pharma sector list in relative terms. However, its liquidity was at a relatively meager EUR 17.5mn. In this respect, only its local peer Antibiotice posted a worse performance, with trading volume at a mere EUR 8.8mn in 2009. Richter (as anticipated) kept its leadership, with shares worth EUR 1,600.4mn changing hands in 2009. Although Krka lagged well behind its Hungarian peers in terms of liquidity, it maintained its critical importance for its home Ljubljana bourse. With its EUR 211.5mn trading volume, Krka accounted for 29.4% of LJSE turnover in 2009.

CEE pharma stocks liquidity in 2009



Source: Erste Groups Research, local stock exchanges

Hungarian pharma stocks liquidity developments in 2009 (EUR mn)



Source: Budapest Stock Exchange

Going forward, we believe that Hungarian pharma stocks will retain their position as the preferred exposure to the CEE pharma sector, keeping reasonable liquidity and solid stock performance, driven by steady business progress. The news flow around the R&D progress might add more shine to Richter, while Egis keeps its attractiveness, due to its persisting valuation gap. Krka is still sidelined, due to its comparatively low liquidity, although the company is ready to address the issue, possibly via a foreign stock exchange listing, should the conditions on its home market not change this year. (Contrary to earlier days, the company has recently been mulling a listing in Warsaw.) Finally, as before, we assume that market participants will also this year be ready to forgive Bioton its temporarily bleak reports, provided that the company does not move from its firmly stated strategic goals and delivers the first tangible restructuring results, including the disposal of certain assets and planned close partnership with Polpharma. Out of the two Romanian pharmas, we believe that Biofarm has all prerequisites to keep its edge over its rival Antibiotice, not only in the company's business results (with better profitability parameters), but also in terms of its stock liquidity, which keeps enjoying support from key shareholders – SIFs, keen to further increase their stake in Biofarm (with the intention to sell it later to a strategic investor).

CEE pharma shares offer attractive upside potential

Company	Currency	Current Price (LC)	1-year-high (LC)	Current price vs 1 y-high (%)	Target price (LC)	Upside potential (%)
Antibiotice	RON	0.645	0.800	-19.4%	0.624	-3.2%
Biofarm	RON	0.211	0.255	-17.6%	0.222	5.1%
Bioton	PLN	0.20	0.35	-42.9%	0.21	3.4%
Egis	HUF	18,850	21,800	-13.5%	21,755	15.4%
Krka	EUR	65.8	76.5	-14.0%	92.0	40.0%
Richter Gedeon	HUF	41,200	44,000	-6.4%	48,200	17.0%

Based on closing prices as of February 1, 2010; Source: Erste Group Research

CEE pharma markets long-term potential untouched by economic slowdown…

…although tightening resources will temper growth in short run…

The 2009 interim results of the CEE-based pharmaceutical companies confirmed that pharma markets are one of the least affected by the economic recession. While regulatory pricing pressures are a regular part of the pharmaceutical business and the top CEE generics players are ready to cope with them, the volatile regional currency fortunes brought additional woes, more difficult to resist, especially in the short term. Reflecting the tightening reimbursement rules, 2009 growth was in most CEE countries tempered to a single-digit pace and, in markets hard-hit by a currency slump, it dived temporarily into negative territory. However, the improvements in the course of the year were clearly visible. The outlook is more encouraging and CEE pharma companies can anticipate restoration of growth in all major regional markets, including those hit hardest this year, such as Ukraine. The low comparative base will be supportive, namely in the first half of 2010, as well. Importantly, after the somewhat challenging 2009, the economic recovery in the CEE region speaks in favor of a return to the catch-up effect, which, along with demographic factors (such as ageing populations), increasing public healthcare awareness and never-ending progress in bringing innovative medicines to the market (including those addressing poorly treated diseases) should propel CEE pharma markets in the coming years. While the future economic growth will also spur greater resources available for healthcare, the cost-conscious approach of healthcare providers is unlikely to change, demanding the most economic drug reimbursement policies. On one side, this speaks in favor of generics producers. On the other hand, the pressure on their price-competitiveness will further intensify.

…as evidenced by cost savings measures in Czech market…

The currently less favorable macroeconomic conditions (with high unemployment rates and hence reduced contributions to the healthcare system) have been provoking short-term cost containment measures as well. In the Czech Republic, as part of an anti-crisis savings package in the budget for 2010, it was agreed that the maximum prices for medicines will be reduced by 7%, while the same cut will be applied to drug reimbursement. Although the maximum prices were in most cases not fully used by manufacturers in the past, the reimbursement amount cut will save money for health insurance providers, but increase the burden for patients and put additional pressure on manufacturers to slash prices (and hence co-payments) in order to defend their competitive positions on the market. The measure was declared as temporary, i.e. valid for one year, but its consequences will undoubtedly be more long-lasting. The first evidence is that it already started to reshape the market, with manufacturers sharply increasing prices of products wherever (given the competitive position) possible before the end of 2009.

…introduction of new reference pricing system in Hungary…

In the course of 2009, it became apparent that the Hungarian pharmaceutical market was getting out of the doldrums. While the quarterly revisions still resulted in a gradual lowering of reference prices, with necessary price adjustments to be done by pharma manufacturers wanting to keep the reimbursement status of their products getting marginal over time. In addition, there was a change for the better in 2009, as the maximum limit for the difference between the price of the product retaining its reimbursement status and the reference drug was moved from 120% to 130%. All told, after the initial worries, the updated guidance from Hungarian pharma companies was raised. At the beginning of the year, Richter refrained from providing any guidance, but in May the company projected its Hungarian market sales stopping their fall and stabilizing y/y in 2009, while in November it did not rule out low single-digit growth. Egis confirmed that its domestic sales tempo should pick up from the 1.4% y/y posted in fiscal year 2008/09 to around 5% y/y in 2009/10. Furthermore, the recent data shows that companies should not be concerned about overspending of the National Health Insurance Fund (OEP) budget. According to the Ministry of Finance, the 2009 expenditures on reimbursed medicines amounted to HUF 343.2bn, just 0.04% above the budget. In this context, it is worth mentioning that, while in 2009 Richter and Egis paid an estimated HUF 2bn and HUF 1.8bn, respectively, to the state budget in rebate and sales rep fees, the legislation changes will start to work in the opposite direction here. Based on a new Hungarian government program aimed at supporting the R&D-oriented pharmaceutical industry, drug producers will have the possibility to reduce their payments to OEP (stemming from a 12% drug subsidy rebate and fees for sales reps) by up to 20% in 2009 (to be paid back by the state in 2010) and up to 100% (to be paid back in 2011) if they spend the saved amount on research and development activities. With respect to their sizable R&D budgets, both Richter and Egis will be able to take full advantage of the program (and trim their costs).

The international reference pricing system, linking the reimbursement level to the average price of the product in the selected (cheapest markets) is the favored idea of CEE regulators these days (with a theoretical deadlock coming nearer, the more CEE states opt to apply it). Recently, it was added to the repertoire of the Hungarian cost savings measures, casting a shadow over the earlier somewhat rosier 2010 market outlook. The new legislation sets the benchmark for reimbursement at the average price of the same drug in five EU countries with the lowest prices. If the Hungarian price exceeds the limit by 30% or more, either the product will be scrapped from the subsidy list or the company will have to enter with the state into an agreement on reimbursement and volumes of supplies of the product for the Hungarian market (putting indirect pressure on the reimbursement rate). The price list will be reviewed once a year. The detailed measures (in a special decree) are yet to be announced; the currency recalculation represents another unknown factor.

…and sales clawback system in Romania

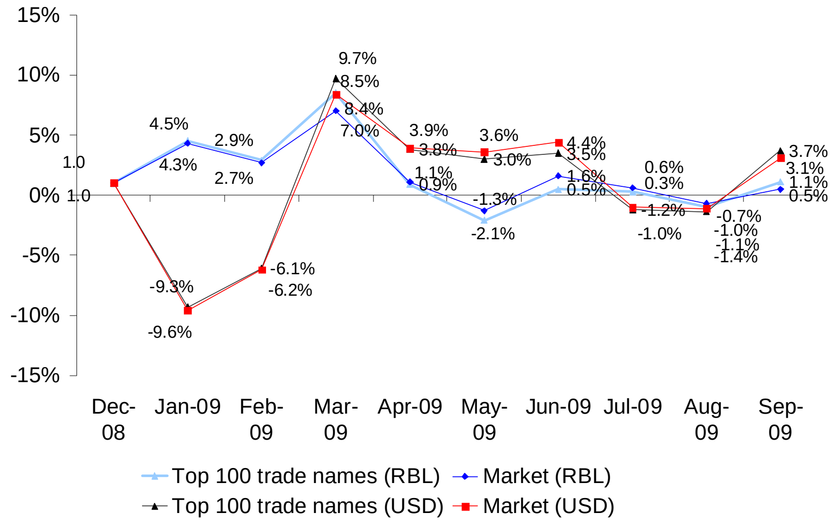
In Romania the restrictive measures were enriched in October 2009 by the introduction of a sales tax amounting to 5% to 11% of sales, depending on turnover. The aim of the new legislation was to bring more balance into the healthcare budget, but the effect is clearly a drain on the results of Romanian pharma companies, which have relatively low exports and are largely dependent on their home market fortunes. Contrary to earlier expectations, the initially proposed mechanism of the clawback system did not get the approval of the Senate by January 25, 2010, the supposed deadline for payment of the sales tax on 4Q09 sales. Nevertheless, while the methodological norms are still not settled, we continue to assume that the sales tax will be applied this year, with its harming effect palpable, particularly in Antibiotice and Biofarm’s 2010 results.

Russia / CIS poised for recovery in 2010

Russia / CIS is set to remain a crucial market for CEE-based pharma companies. As its share in total sales sometimes exceeds that of the home country, the developments in the area are carefully watched by market participants. The economic crisis, with sharp ruble and other former CIS countries’ currency depreciation, dramatically threatened CEE pharmas’ fortunes at the beginning of 2009. Fortunately, over the course of the year, the situation gradually improved and further recovery is in the cards, with a low comparative base effect promising to give an additional lift to the 2010 figures.

Reflecting the looming uncertainties on the market, as well as the paralyzing forex impact, the Russian commercial pharmaceutical market contracted by 13.5% in ruble terms and by 25% in US dollar terms in January 2009 compared to December 2008 (based on DSM Group data). As the price hike corresponding to the ruble depreciation pace would be too much for patients to fully absorb, CEE-based Russia/CIS players, if they wanted to keep their sales moving, had no choice but to at least partly share the currency related burden with wholesalers. With contracts with wholesalers fixed in US dollars or euro, CEE pharma manufacturers had to offer their partners higher discounts (related to the forex rate), while extending credit terms to the reliable ones. Nevertheless, the situation stabilized in the following months. After the steep fall at the beginning of the year, the ruble continued in its stabilization starting from 2Q, boding well for steadier pricing levels, as well as diminishing forex related discounts provided by CEE companies to their wholesale partners in Russia. According to DSM Group data, in 1-3Q09, the Russian commercial pharmaceutical market advanced by a hefty 25% y/y in ruble terms to RBL 157bn, while the market volume (number of packages sold) shrank by 8.7% y/y. The prices of medicines went up by 15.8% in the January – September 2009 period; the imported drug price increase of 18.3% was well ahead of the rise of domestic products (up by 8.4%) in the same time. All of this was mirrored in the mixed sales performance of key CEE-based pharma players in Russia in the first nine months of 2009. (Y/y flat sales were reported by Krka, a 4% y/y tempo was posted by Egis, with a 7.5% y/y rise by Richter, all in euro terms.)

Changes in prices of drugs on the Russian commercial pharmacy market



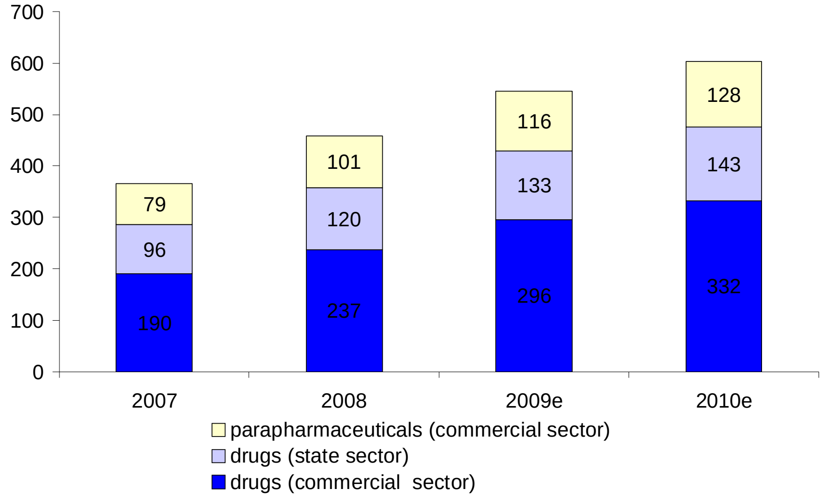
Source: DSM Group

Going forward, apart from the general economic environment, possible regulatory changes will remain in focus. The price monitoring introduced in May 2009 has been widely assumed to be the first step in the stricter (and, in contrast with past practice, enforced) drug price regulation in Russia. In 2010, prices of drugs from the "essential list" covering life-threatening conditions will be more strictly controlled, with limited maximum markups further curbing the state expenditures on medicines. Manufacturers are obliged to submit for registration retail prices of all their products on the essential list until April 1, 2010. (The essential list comprises around 500 INN names, corresponding to around 5,400 trade names [out of the total 17,000 registered trade names on the Russian market in 2009]). Needless to say, the reimbursed segment is relatively small compared to other regional markets, with Russian patients funding purchases of medicines from their own pockets. (It is estimated that reimbursed drugs account for less than 30% of total Russian drug consumption.) In addition, as the essential list's product prices will be revised only once a year, it is widely anticipated that producers will tend to register rather elevated prices in order to cover for possible unfavorable developments later in the course of the year, including currency risks. The price increases in the non-regulated part represent another way to compensate for eventually shrinking margins in the regulated segment. Hence, much more important from the consumer perspective would be an efficient system addressing the huge differences in markups of wholesalers and retailers (which can be only partly justified by logistics across the country). (Wholesale markups are currently reportedly ranging from 15% to 60%, while retail pharmacy markups reach from 15% to 100%.)

The steadily rising prices of medicines (driven by imports, accounting for an estimated 79% of final drug consumption and nearly 100% of API needs) have also provided more ammunition for Russian authorities trying to reduce the dependence of the country on pharmaceutical imports and support the domestic pharma industry. While the wording is strong, the action plan is vague and, in reality, with the pharmaceutical industry in private hands (including foreign participation), the situation is difficult to change. Also, the plans to introduce a nationwide obligatory health insurance system are still in a nascent stage and it is difficult to see how they will change the market dynamics. All told, at the moment, CEE companies do not anticipate that their business conditions in Russia will change significantly in the near term. With their orientation primarily on the private segment and established local manufacturing bases (with the possibility to scale up operations if necessary), they do not see the tougher rules endangering their position. 2009 turned attention once again to currency developments as one of the crucial factors of successful business performance among exporters to the Russian pharma market. From this perspective, the market outlook is promising, as the ruble gained ground and the country's economic environment is once again bolstered by rising oil prices (from their 2009 lows).

Consequently (helped also by the low comparative base), a return to a pre-crisis double-digit sales tempo in Russia could be a realistic target for CEE producers in 2010. Similarly, while the burden of the economic slowdown is heavier and forex developments less encouraging, the situation in other CIS markets should improve as well. After bottoming out in 2009, sales should record at least a modest recovery in 2010.

Russian pharmaceutical market outlook (RBL bn)



Source: DSM, in final consumer prices

2009 saw Zentiva's farewell Sopharma's Warsaw stock exchange listing should bring company under spotlight in 2010

The year 2009 did not see any major M&A activity originated by CEE pharma players. Hence, the biggest deal in the regional pharma universe remained the takeover of Czech-based Zentiva by Sanofi-Aventis, a transaction that was initiated in the pre-crisis period. As a result of the successful bid (valuing Zentiva at CZK 43.9bn, or EUR 1.66bn), the company was subsequently delisted from the Prague (as well as London) Stock Exchange in April 2009. The step has reduced the number of investable CEE pharma titles. While no new listing from the CEE pharma universe is on the agenda now, interesting information for investors is the intention of Bulgaria's Sopharma to list its shares (in parallel to its home Sofia bourse) in Warsaw, one of the region's most liquid markets. The relevant paperwork is in progress, the prospectus was already approved and, should the move be accompanied (apart from higher stock turnover) by better transparency for international investors, we will initiate our coverage of the stock in due time.

Regional M&A in 2010: Serbian Galenika on block

Going forward, CEE pharma leaders maintain their interest in the M&A area. Nonetheless, a brief look at the list of declared objectives (no need for additional capacities in generics manufacturing, interest in attractive niche /biological products alongside a reasonable/affordable price tag) are difficult to be met by candidates in the region. After several postponements, the sale of Serbia's Galenika, the only sizable publicly announced privatization transaction in the region, should kick off in 1Q10. The deadline for submitting pre-qualification bids was set by Serbia's Privatization Agency for February 19, 2010. Bidders are required to have at least five years of experience in the pharmaceutical industry and 2008 revenues from sales of pharmaceutical products of more than EUR 100mn. Financial investors that had more than EUR 250mn in managed assets in 2008 are also allowed to submit offers. Reportedly, none of the CEE-based players is among the interested parties (which include, according to media information, Germany's Stada and Greece's Alapis). While Russia/CIS retains its appeal, with a sound long-term tempo to be driven by the persistent gap in spending on pharmaceuticals and healthcare between the country and the CEE region (not to mention Western European levels), the legal and regulatory framework speaks in favor of expanding existing greenfield operations. As CEE-based pharma manufacturers are starting to look beyond their traditional CEE horizons, Turkey (an attractive combination of relatively low per capita drug spending, big population and strong generics sales growth) is becoming a new hotspot, with possibilities there to be increasingly explored by CEE-based leaders. Finally, the two small Romanian pharma companies are most likely to end up on the opposite side of the transaction block. The timing is difficult to predict, but currently it is assumed that Biofarm should find a strategic owner only in 2011, while Antibiotice's fortunes will depend on the formation of a new conglomerate under state control (with a rather cloudy shape at present).

CEE currencies vs. US dollar, euro in 4Q09 and in 2009

	4Q08 average USD	4Q08 average EUR	4Q09 average USD	4Q09 average EUR	4Q 09 y/y USD	4Q 09 y/y EUR	4Q09 vs 3Q09 USD	4Q09 vs 3Q09 EUR
Hungarian forint	199.4	262.4	183.3	270.9	8.8%	-3.1%	3.5%	0.1%
Czech crown	19.2	25.3	17.5	25.9	9.8%	-2.2%	2.1%	-1.2%
Polish zloty	2.9	3.8	2.8	4.2	1.3%	-9.7%	3.9%	0.5%
Romanian leu	2.9	3.8	2.9	4.3	0.2%	-10.6%	2.3%	-1.0%
Russian rouble	27.3	36.0	29.5	43.6	-7.5%	-17.4%	6.3%	2.8%
Ukrainian hryvnia	6.2	8.2	8.0	11.8	-22.3%	-30.4%	-2.2%	-5.3%

	2008 average USD	2009 average USD	2009 average y/y USD	2008 average EUR	2009 average EUR	2009 average y/y EUR
Hungarian forint	172.1	202.3	-14.9%	251.5	280.6	-10.4%
Czech crown	17.0	19.1	-10.6%	24.9	26.4	-5.7%
Polish zloty	2.4	3.1	-22.7%	3.5	4.3	-18.7%
Romanian leu	2.5	3.0	-17.4%	3.7	4.2	-13.1%
Russian rouble	24.8	31.7	-21.7%	36.4	44.1	-17.5%
Ukrainian hryvnia	5.3	7.8	-32.4%	7.7	10.9	-29.1%

Source: Erste Group Research, National Banks' statistics

As sales of Richter, Egis and Krka in certain CEE markets are invoiced in local currencies (and even if the invoice is in euros, the local reimbursement systems set prices in local currency), the regional currencies' depreciation (especially at the beginning of 2009) harmed their top line. Nevertheless, developments took a turn for the better, particularly in the second half of 2009, boding well for sales improvements. In particular, all of the CEE-based Russian market players benefited from the ruble stabilization, helping - along with the brightening economic outlook (boosted once again by rising oil prices) - to bring business conditions there to a normal level. While Krka, with its mostly euro-incurred costs and export revenue exposure to the CEE region, suffered most, the Hungarian manufacturers (with costs predominantly in HUF and strong shares of exports) enjoyed a much better position. Despite the ongoing appreciation in 4Q09, the forint remained weaker y/y vs. the euro (and US dollar) in 2009, boding well for the full-year 2009 results of Hungarian pharmaceutical companies. While the Polish zloty made a rather bold move in the second half of the year, for FY09, the Polish currency was one of the weakest performers and zloty depreciation put a heavy lid on sales of CEE-based pharmas, including the Hungarian ones. The appreciation of the forint was only marginally less steep than we expected at the time of our last sector report (November 2009), and we make only minor adjustments to our currency forecasts for 2009 and coming periods for Richter and Egis. Here we want to emphasize that, after the turbulent 2009, we continue to envisage 2010 to be calmer, with only minor changes on the interim basis, speaking in favor of smoothening financial results for both Hungarian companies in the course of 2010.

Hungarian forint developments

average	1Q09	2Q09	3Q09	4Q09	1Q10e	2Q10e	3Q10e	4Q10e
HUF / EUR	294.2	285.9	271.3	270.9	275.0	272.0	268.0	265.0
HUF / USD	226.2	210.2	189.7	183.3	185.8	176.6	176.3	180.3
end od period	**1Q09**	**2Q09**	**3Q09**	**4Q09**	**1Q10e**	**2Q10e**	**3Q10e**	**4Q10e**
HUF / EUR	309.2	272.4	270.4	270.8	270.0	270.0	265.0	265.0
HUF / USD	233.0	193.3	184.8	188.1	176.5	174.2	176.7	182.8

Source: NBH, forecasts Erste Group Research

Changing regional currency situation and fine-tuning of risk-free rates (reflecting moves in government bond yields) to be incorporated into our models

Since the publication of our last CEE pharma sector report in November 2009, interest rates in major world economies have not seen major changes, as their historically low levels (with the US Federal Reserve key interest rate at the unprecedented range of zero to 0.25% and the European Central Bank's interest rate of 1.25%) did not provide any room for further cuts. On the other hand, CEE countries (particularly the Czech Republic, Hungary and Romania) used the maneuvering space for minor downward corrections of rates. The external indebtedness of CEE pharma companies continues to be minimal and their investment plans do not rely on tapping financial markets. Consequently, the relatively tight availability of credit resources has not been endangering their financial results. Thus, the main factors we have to reconsider in our models are the applied equity risk premiums and risk-free rates, as well as changing currency forecasts.

Our methodology for setting equity risk premiums, linked to the respective country's S&P long-term foreign currency rating that we introduced in our pharma sector report in May 2009, remains unchanged. In summary: 4.5% is used as a base equity risk premium (mirroring the long-term outperformance of stocks vs. bonds), 25bp is added for each rating notch below AAA and 40bp is added for each rating notch below investment-grade (i.e. below BBB-). For perpetuity, extra charges are trimmed to 20bp and 35bp, respectively (while still based on the current rating). Since our last report, there have not been any changes in the relevant home country ratings, so the application of the methodology keeps punishing to a certain extent the two Hungarian companies, with the resulting equity risk premium well above other regional peers', particularly that of Krka. While we believe that the Hungarian macroeconomic picture will continue to stabilize and government bond yields are still on a descending path in Hungary, in our Richter and Egis DCF models, we leave our earlier assumptions (the risk-free rate of 7.0%) untouched. At the same time, we opt to remain on the conservative side and stick to the risk rates for Poland and Slovenia at the same level as in our previous report from November 2009 (6.0% and 4.4%, respectively). Reflecting lowering government bond yields in Romania, we reduced the risk-free rate for the detailed forecast period to 8.0% (from 10%).

4Q09 results preview

CEE pharma reporting schedule

Date	Company	Release / event
week of February 8, 2010	Richter Gedeon	2009 results
10.2.2010	Egis	1Q2009/10 results
12.2.2010	Biofarm	2009 results
15.2. 2010	Antibiotice	2009 results
25.2.2010	Krka	2009 results
1.3.2010	Bioton	2009 results

Source: Erste Group Research, company data

Antibiotice: The company is scheduled to report its preliminary FY09 results on February 15, 2010. We expect the company to post sales of RON 225.8mn, up 4.6% y/y in 2009. Backed by an average 11% increase in the company's drug prices, Antibiotice's sales on the domestic market are envisaged to advance by 3.5%y/y in 2009. (Due to the change in rules for calculation of reimbursed drug prices, starting from April 2009, Antibiotice's drug prices went up by 15%, offsetting the drop in drug consumption, which we estimate at some 7%). Helped by the RON weakening, Antibiotice's export tempo is foreseen to reach 6% y/y in RON terms. Although we estimate the forex burden to be lower y/y in 4Q, similarly to the previous year, the 4Q09 financial result is projected to end in red numbers and drag the bottom line into negative territory. We forecast the 4Q09 net loss shrinking y/y to RON 3.5mn (vs. RON 6.4mn in 4Q08). Nevertheless, with respect to the previous period's more optimistic picture, this translates into net profit of RON 15.5mn, up 47% y/y for FY09.

Biofarm: The company is scheduled to report its FY09 preliminary results on February 12, 2010. We expect 4Q09 sales to slip by 2% y/y to RON 17.8mn, reflecting the company's more conservative stance, with a focus on the collection of receivables. Although the core business segment of Biofarm - OTC drugs – was negatively affected by the drop in demand caused by the economic slowdown, the high brand awareness, supported by intense marketing, as well as the company's highly competitive prices, boded well for a solid sales performance in 2009 and we anticipate the 2009 sales figure at RON 68.4mn, up some 5% y/y. The year-earlier low comparative base creates big room for improvement on both the operating and bottom lines. For the latter, the most decisive factor is the changing equity market situation. While in the year-earlier period the company was forced to make a huge provision, due to the depreciation of its stock portfolio, 4Q09 saw a turnaround, with at least a partial provision reversal, boosting 4Q09 net profit. In summary, assuming a RON 6.0mn provision reversal, we expect 4Q09 net profit to surge to RON 6.6mn, pushing up the 2009 net profit to RON 18.9mn.

Bioton: Bioton's 4Q09 results will be published at the end of the official deadline, i.e. on March 1, 2010. We forecast the company posting a 4Q09 net loss of PLN 25.2mn on sales of PLN 73.0mn, translating into a 2009 net loss of PLN 75.3mn on sales of PLN 290.3mn (consolidated and according to IFRS standards). Helped by the low comparative base, Bioton's sales are estimated to rise by some 21% y/y to PLN 73.0mn in 4Q09. Nonetheless, we expect the sales slipping by 1.1% y/y on a cumulative basis in 2009, as the first-time consolidation effect (the two Italian companies and MJ Bioton Life Sciences have been consolidated since 2Q08) will be insufficient to counterbalance the absence of a one-off payment related boost in the year-earlier comparative base. The subdued profitability parameters of the newly consolidated companies and mounting restructuring costs (including further write-offs in addition to severance payments linked to staff cuts) are anticipated to continue to drag the operating line into red territory. We forecast the operating loss expanding to PLN 74.6mn in 2009, out of which the fourth quarter is anticipated to add an operating loss of PLN 19.4mn. Furthermore, despite the y/y improving financial result, the bottom line is set to stay in the red. Nonetheless, with 4Q08 weighed down by a huge write-off at Bioton Wostok, we envisage the net loss narrowing y/y to PLN 25.2mn in 4Q09; for 2009, we project a net loss of PLN 75.3mn, a much better figure than the year-earlier net loss of PLN 218.9mn.

Egis: Egis is scheduled to announce its 1Q09/10 report on February 10, after the market close. The year-earlier high comparative base (hiked by one-off effects in Poland) does not leave much room for y/y improvements on the top line. Thus, despite the benefits from the stabilization of the Hungarian pharma market, as well as the y/y recovering Russia/CIS sales, we anticipate Egis' 1Q09/10 sales retreating by 12.2% y/y to HUF 25,284mn. As the y/y shrinking bulk chemicals sales' supportive effect for margins will be largely erased by the y/y less favorable currency fortunes in the period, as well as the absence of one-off effects (linked to the one-off boost to Polish sales in the previous year's period), the company is expected to deliver a rather uninspiring y/y performance on the operating line (down 40% y/y to HUF 3,296mn). On the other hand, the q/q stabilizing forint bodes well for the y/y improvement in the financial result. In summary, with respect to the slump in EBIT, we forecast a 30.6% y/y drop in net profit to HUF 3,855mn in 1Q09/10.

Krka: Krka's 2009 results are scheduled for release on February 25, after the market close. As Krka published its consolidated sales highlights ahead of its full report, we do not anticipate any major surprises on the top line. Reflecting the slowdown in Russia/CIS as well as in Western European markets (the latter due to delays in product launches), Krka's 2009 sales remained nearly flat y/y at EUR 951mn. CEE markets continued to be the main engine of growth, with sales there rising by a sound 6% y/y. Krka's gross and operating profitability parameters were compromised by persistent (albeit already receding gradually in the course of the year) pressures from the strength of the euro vs. regional currencies in 2009. Nevertheless, reflecting the recently revealed information about the provision reversal, we project Krka's operating profit to increase by 7.0% y/y to EUR 253.5mn, with net income up 12.1% y/y to EUR 174.8mn in 2009.

Richter Gedeon: As per tradition, the company did not disclose the exact date for the publication of its 4Q09 figures; it is expected that it will deliver them in the second week of February (February 9-11). We envisage Richter's consolidated sales advancing by 2.7% y/y to HUF 66,915mn in 4Q, lifting the 2009 sales up 11.6% y/y to HUF 263,989mn. The still buoyant US fortunes (benefiting from the drospirenone profit sharing agreement) along with recovering Russian sales are anticipated to offset the sluggishness of EU markets (in particular, certain CEE markets, like Poland, with sales hampered by currency developments). While the year-earlier low comparative base bodes well for y/y progress on the operating level, for the financial result, the opposite is the case. All told, we forecast net profit falling by 24.6% y/y to HUF 10,548mn in 4Q09, bringing 2009 net profit to HUF 47,839mn (up 15.5% y/y).

4Q09 results preview summary

Antibiotice

RAS	4Q2009e	4Q2008	y/y	1-4Q2009e	1-4Q2008	y/y
Total sales (RON mn)	68.05	60.39	*12.7%*	225.84	215.81	*4.6%*
Operating profit (RON mn)	4.08	2.39	*70.7%*	29.34	25.35	*15.8%*
Net income (RON mn)	-3.46	-6.36	*n.m.*	15.54	10.57	*47.0%*
Operating margin	*6.0%*	*4.0%*		*13.1%*	*11.3%*	
Net margin	*-5.1%*	*-10.5%*		*6.9%*	*4.7%*	

Biofarm

RAS	4Q2009e	4Q2008	y/y	1-4Q2009e	1-4Q2008	y/y
Total sales (RON mn)	17.76	18.13	*-2.0%*	68.36	65.10	*5.0%*
Operating profit (RON mn)	2.96	1.07	*175.5%*	14.15	14.55	*-2.8%*
Net income (RON mn)	6.57	-33.63	*n.m.*	18.94	-21.31	*n.m.*
Operating margin	*16.7%*	*5.9%*		*20.6%*	*22.0%*	
Net margin	*37.0%*	*-185.5%*		*27.6%*	*-32.2%*	

Bioton

IFRS consolidated	4Q2009e	4Q2008	y/y	1-4Q2009e	1-4Q2008	y/y
Total sales (PLN 000)	73,041	60,403	*20.9%*	290,284	293,517	*-1.1%*
Operating profit (PLN 000)	-19,366	-90,806	*-78.7%*	-74,605	-71,487	*4.4%*
Net income (PLN 000)	-25,158	-181,736	*-86.2%*	-75,294	-218,892	*-65.6%*
Operating margin	*-26.5%*	*-150.3%*		*-25.7%*	*-24.4%*	
Net margin	*-34.4%*	*-300.9%*		*-25.9%*	*-74.6%*	

Egis

IFRS nonconsolidated	1Q 09/10e	1Q 08/09	y/y
Net sales (HUF mn)	25,284	28,792	*-12.2%*
Operating profit (HUF mn)	3,296	5,490	*-40.0%*
Net income (HUF mn)	3,855	5,555	*-30.6%*
Operating margin	*13.0%*	*19.1%*	
Net margin	*15.2%*	*19.3%*	

Krka

IFRS consolidated	4Q2009e	4Q2008	y/y	1-4Q2009e	1-4Q2008	y/y
Total sales (EUR 000)	261,135	261,982	*-0.3%*	951,009	949,920	*0.1%*
Operating profit (EUR 000)	98,582	84,962	*16.0%*	253,467	236,781	*7.0%*
Net income (EUR 000)	66,406	45,126	*47.2%*	174,770	155,955	*12.1%*
Operating margin	*37.8%*	*32.4%*		*26.7%*	*24.9%*	
Net margin	*25.4%*	*17.2%*		*18.4%*	*16.4%*	

Richter

IFRS consolidated	4Q2009e	4Q2008	y/y	1-4Q2009e	1-4Q2008	y/y
Total sales (HUF mn)	66,915	65,150	*2.7%*	263,989	236,518	*11.6%*
Operating profit (HUF mn)	10,590	6,366	*66.4%*	47,179	34,156	*38.1%*
Net income (HUF mn)	10,548	13,987	*-24.6%*	47,839	41,410	*15.5%*
Operating margin	*15.8%*	*9.8%*		*17.9%*	*14.4%*	
Net margin	*15.8%*	*21.5%*		*18.1%*	*17.5%*	

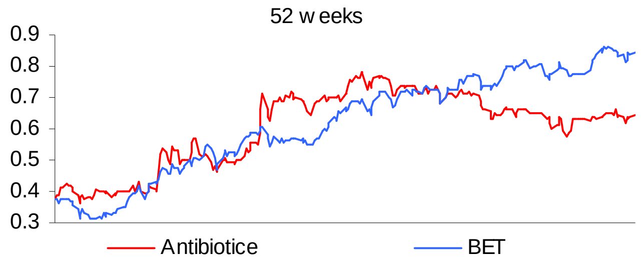
Source: Erste Group Research

Company Report – Pharmaceuticals – Romania – February 3, 2010

Antibiotice Reduce

Raluca Ungureanu, +4021 311 27 54 raluca.ungureanu@bcr.ro

RON mn	2008	2009e	2010e	2011e
Net sales	215.8	225.8	242.6	263.1
EBITDA	38.8	42.7	39.3	51.7
EBIT	25.3	29.3	24.2	36.0
Net result after min.	10.6	15.5	17.0	26.0
EPS (RON)	0.02	0.03	0.04	0.06
CEPS (RON)	0.05	0.06	0.07	0.09
BVPS (RON)	0.54	0.58	0.63	0.71
Div./share (RON)	0.02	0.02	0.01	0.02
EV/EBITDA (x)	5.0	8.4	9.0	6.5
P/E (x)	15.5	18.9	17.2	11.3
P/CE (x)	7.2	10.1	9.1	7.0
Dividend Yield	4.6%	2.6%	2.3%	3.5%



Performance	12M	6M	3M	1M
in RON	78.7%	-6.5%	-3.0%	2.4%
in EUR	88.0%	-3.4%	2.4%	6.2%

Share price (RON)	0.65	Reuters	ATBE.BX	Free float	37.0%
Number of shares (mn)	454.9	Bloomberg	ATB RO	Shareholders	Ministry of Health (53.0%)
Market capitalization (RON mn / EUR mn)	293 / 72	Div. Ex-date	07/05/09		SIF Oltenia (10%)
Enterprise value (RON mn / EUR mn)	360 / 88	**Target price**	**0.624**	Homepage:	www.antibiotice.ro

Outlook still gloomy

- **We have updated our 5-year DCF valuation of the company in order to reflect the impact of the lower risk-free rate, as well as the worsening payment conditions in the market, with the period for collecting receivables rising to 300 days or more. As a result of the adjustments, we slightly raise our target price to RON 0.624 per share (from RON 0.615) but maintain our Reduce recommendation.**

- **The dramatic situation on the local pharma market, with the state not paying for reimbursed drugs since June 2009, has made us more cautious in terms of working capital management. We remain conservative and assume an improvement of the cash conversion cycle only starting next year.**

- **The company has not managed so far to start exports of finished products to the US market, but this is only a matter of weeks away. This was one of the assumptions we employed when forecasting an improvement in working capital management starting this year, as payments in foreign markets are made significantly faster (90 days) than in the domestic market.**

- **We have adjusted our estimates for FY09 in order to reflect the slightly better than expected 3Q09 results, but also some changes in the assumptions underlying the 4Q09 forecasts: the higher than anticipated depreciation of the local currency (with a negative impact on raw material expenses) and the delays in implementing the clawback system (tax on sales of Rx drugs, sales to hospitals and within national health programs which we estimate at 9% for the company).**

Changes in forecast/outlook

Slightly better operating performance in 4Q09

We have revised our estimates for FY09 in order to account for the better than expected result for 1-3Q09, but also for the substantial changes in the assumptions underlying our forecast for 4Q09, as result of the clawback system not being implemented on October 1, 2009. Recall that the Romanian authorities decided last fall to charge a tax ranging between 5% and 11% on sales of Rx drugs, sales to hospitals and within national health programs. The initially proposed mechanism of the clawback system did not get Senate approval by January 25, 2010, which was supposed to be the deadline for payment of tax on 4Q09 sales. Furthermore, the methodological norms for applying this tax have not been settled yet.

No provisions recorded for tax on sales

Based on our discussions with management, no provisions were recorded in 4Q09 for this tax. We decided to assume this guidance, as the clawback system is unlikely to affect the 2009 figures.

We have also adjusted material costs upward for 4Q09, in order to account for the local currency development against the EUR and USD, as imports account for roughly 70% of the company's raw material acquisitions.

4Q09 EBIT of RON 4.08mn

We arrived at EBIT of RON 4.08mn for 4Q09, some RON 0.36mn higher than our previous estimate. We also base our expectation of a better last quarter on the fact that management was more prudent on the expenses side, in order to offset the negative impact of the tax on sales.

The financial loss was also adjusted, with the new forecast pointing to a higher financial loss of RON 10.4mn (previously RON 6.5mn). The estimate reflects a rather conservative judgment regarding management's ability to deal with FX issues. The company does not employ hedging, but it strives to correlate cashing and payments in foreign currency in order to minimize the FX risk.

Change in estimates

RAS	2009e			2010e		
(RON, mn)	Now	Before	*Change*	Now	Before	*Change*
Net sales	225.8	225.4	*0.2%*	242.6	245.1	*-1.0%*
Total revenues	224.5	231.6	*-3.1%*	248.8	251.4	*-1.0%*
Material costs	69.8	64.7	*7.8%*	64.4	65.1	*-1.0%*
Personnel costs	62.9	64.2	*-2.0%*	66.3	66.3	*0.0%*
Other operating expenses	50.4	65.2	*-22.7%*	80.8	81.6	*-1.0%*
EBITDA	42.7	39.1	*9.2%*	39.3	40.4	*-2.8%*
EBIT	29.3	25.7	*14.0%*	24.2	25.3	*-4.4%*
Financial result	-10.4	-6.5	*59.3%*	-3.5	-4.3	*-19.9%*
Net income	15.5	16.1	*-3.7%*	17.0	17.7	*-3.5%*

Source: Erste Group Research

Sales to increase at CAGR of 8.7% over 2010-14

We maintain our estimates regarding sales growth over the period 2010-14 at a CAGR of 8.7%, on the back of some 8-9% increase in sales on the local market. We expect exports to advance at a CAGR of 18%, mainly on the back of starting exports of finished products to the US market. Recall that Antibiotice has inked a contract with an annual value of USD 15mn with a US partner (ACIC) for the sale of finished products on the US market. However, the company was not yet granted FDA certification, which is mandatory to start this business partnership. Although the company's expectations were that the export of finished products to the US market would start by the end of 2009, to be conservative, we have assumed this happening in 2010. Thus, for the time being, no adjustments are necessary, due to this delay.

We maintain our cautious stance on the company, as it is only a matter of time until the clawback system is implemented. As we lack guidance regarding the mechanism of the clawback system, we assume Antibiotice paying a 9% tax on Rx drugs sales, sales to hospitals and within national health programs.

Likely to sacrifice 2010 margins, rather than marketing and sales programs

This will put significant pressure on the company's margins, especially in the context wherein Antibiotice is running an ambitious marketing and development strategy, with marketing expenses amounting to 24-25% of sales. One of the main goals of the company's strategy is to expand exports, in an effort to balance its cash flow, as payments from foreign partners are made significantly faster (90 days) compared with the situation on the domestic market, where receivables are collected in 10 months. For this reason, we believe that the company would rather sacrifice margins for one to two years than postpone/threaten its sales development strategy.

Tax on sales to put pressure on cash flows

Besides the obvious pressure on operating margins, the tax on sales will put pressure on the company's cash flow in 2010, especially as it should be paid on a quarterly basis (whereas the average period for collecting receivables on the pharma market is 300 days). In this context, it is likely that the company will contract additional short-term loans in order to fund working capital needs.

Operating margin to fall this year, follow ascending path starting in 2011

We maintain our expectations of a decrease in the operating margin in 2010. Starting next year, we expect an improvement in profitability, on the back of good cost control (with the company managing to adjust to the new tax rules) and improvement of working capital management. As we have largely maintained the assumptions underlying the forecasts in our previous report, the new estimates are very close to the previous ones. Thus, the valuation result is not far from the figure presented in our initial coverage report.

Valuation summary

In order to value the company, we have updated our 5-year DCF model, using the same timeframe and only slightly changing some of the assumptions:

- We have reduced the risk-free rate for the detailed forecast period to 8% (from 10% previously), as a result of lowering government bond yields (due to the National Bank reducing the key rate). For perpetuity, in order to be conservative, we maintained the risk-free rate at 6%.
- Beta at 1.1 in the detailed forecast period and 1 in perpetuity.
- The equity ratio remained unchanged at 70% in the detailed forecast period and 75% in perpetuity.
- No changes were assumed in terms of the CAPEX plan.

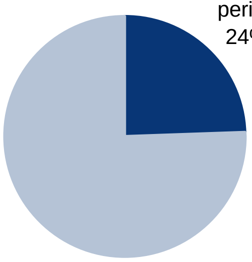
WACC calculation

	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Risk free rate	8.0%	8.0%	8.0%	8.0%	8.0%	6.0%
Equity risk premium	7.2%	7.2%	7.2%	7.2%	7.2%	6.7%
Beta	1.1	1.1	1.1	1.1	1.1	1.0
Cost of equity	**15.9%**	**15.9%**	**15.9%**	**15.9%**	**15.9%**	**12.7%**
Cost of debt	10.5%	10.5%	10.5%	10.5%	10.5%	8.5%
Effective tax rate	25.0%	25.0%	25.0%	25.0%	25.0%	20.0%
After-tax cost of debt	**7.9%**	**7.9%**	**7.9%**	**7.9%**	**7.9%**	**6.8%**
Equity weight	70%	70%	70%	70%	70%	75%
WACC	**13.5%**	**13.5%**	**13.5%**	**13.5%**	**13.5%**	**11.2%**

DCF valuation

(RON mn)	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Sales growth	*7.4%*	*8.5%*	*9.0%*	*9.4%*	*7.2%*	*5.0%*
EBIT	24.2	36.0	41.3	47.6	51.6	54.3
EBIT margin	*9.7%*	*13.3%*	*14.0%*	*14.8%*	*15.0%*	*15.0%*
Tax rate	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*25.0%*	*20.0%*
Taxes on EBIT	-6.1	-9.0	-10.3	-11.9	-12.9	-10.9
NOPLAT	**18.2**	**27.0**	**30.9**	**35.7**	**38.7**	**43.4**
+ Depreciation	15.1	15.7	16.7	18.5	20.3	20.5
Capital expenditures / Depreciation	*101.1%*	*108.9%*	*106.2%*	*102.4%*	*101.0%*	*100.0%*
+/- Change in working capital	-8.6	-5.7	-6.1	-6.5	-4.6	-3.1
Chg. working capital / chg. Sales	*-35.3%*	*-27.1%*	*-25.2%*	*-23.5%*	*-19.8%*	*-18.0%*
- Capital expenditures	-15.2	-17.1	-17.8	-18.9	-20.5	-20.5
Free cash flow to the firm	**9.4**	**19.9**	**23.8**	**28.7**	**33.9**	**40.3**
Terminal value growth						*2.0%*
Terminal value						447.7
Discounted free cash flow - Dec 31 2009	8.3	15.4	16.3	17.3	18.0	233.3
Enterprise value - Dec 31 2009	**308.8**					
Minorities	0.0					
Non-operating assets	0.0					
Net debt	66.7					
Other adjustments	0.0					
Equity value - Dec 31 2009	**242.0**					
Number of shares outstanding (mn)	454.9					
Cost of equity	15.9%					
12M target price per share (RON)	**0.624**					
Current share price (RON)	0.645					
Up/Downside	*-3.2%*					

Enterprise value breakdown



Sensitivity (per share)

Terminal value EBIT margin

WACC	14.0%	14.5%	15%	15.5%	16.0%
10.2%	0.649	0.673	0.698	0.722	0.746
10.7%	0.613	0.636	0.659	0.682	0.704
11.2%	0.581	0.602	**0.624**	0.646	0.667
11.7%	0.552	0.573	0.593	0.613	0.634
12.2%	0.526	0.546	0.565	0.584	0.604

Terminal value growth

WACC	1.0%	1.5%	2.0%	2.5%	3.0%
10.2%	0.624	0.659	0.698	0.741	0.791
10.7%	0.593	0.624	0.659	0.698	0.741
11.2%	0.565	0.593	**0.624**	0.659	0.698
11.7%	0.540	0.565	0.593	0.624	0.659
12.2%	0.516	0.540	0.565	0.593	0.624

Source: Erste Group Research

Income Statement	**2006**	**2007**	**2008**	**2009e**	**2010e**	**2011e**
(RAS, RON mn, 31/12)	31/12/2006	31/12/2007	31/12/2008	31/12/2009	31/12/2010	31/12/2011
Net sales	**195.68**	**229.42**	**215.81**	**225.84**	**242.58**	**263.12**
Invent. changes + capitalized costs	0.44	4.02	9.32	-1.31	6.19	6.72
Total revenues	**196.12**	**233.44**	**225.13**	**224.53**	**248.77**	**269.83**
Other operating revenues	1.69	2.41	1.72	1.31	1.99	2.15
Material costs	-55.00	-61.20	-69.12	-69.79	-64.39	-71.84
Personnel costs	-43.38	-54.85	-64.06	-62.89	-66.29	-67.66
Other operating expenses	-54.15	-68.90	-54.86	-50.42	-80.78	-80.83
EBITDA	**45.27**	**50.90**	**38.80**	**42.74**	**39.29**	**51.66**
Depreciation/amortization	-11.78	-8.82	-13.46	-13.40	-15.08	-15.69
EBIT	**33.49**	**42.08**	**25.35**	**29.34**	**24.21**	**35.97**
Financial result	0.99	-5.19	-11.97	-10.38	-3.45	-4.30
Extraordinary result	0.00	0.00	0.00	0.00	0.00	0.00
EBT	**34.49**	**36.89**	**13.38**	**18.95**	**20.76**	**31.67**
Income taxes	-6.23	-4.43	-2.81	-3.41	-3.74	-5.70
Result from discontinued operations	0.00	0.00	0.00	0.00	0.00	0.00
Minorities and cost of hybrid capital	0.00	0.00	0.00	0.00	0.00	0.00
Net result after minorities	**28.25**	**32.46**	**10.57**	**15.54**	**17.02**	**25.97**

Balance Sheet	**2006**	**2007**	**2008**	**2009e**	**2010e**	**2011e**
(RAS, RON mn, 31/12)						
Intangible assets	0.94	1.77	1.72	1.69	2.19	2.69
Tangible assets	105.85	162.32	163.56	157.57	157.61	168.88
Financial assets	0.01	0.01	0.08	0.08	0.08	0.08
Total fixed assets	**106.79**	**164.10**	**165.35**	**159.34**	**159.88**	**171.65**
Inventories	18.33	21.75	35.95	44.55	46.52	46.86
Receivables and other current assets	106.59	122.33	124.45	179.43	189.41	198.24
Other assets	0.25	0.42	0.31	0.26	0.31	0.33
Cash and cash equivalents	28.67	36.69	42.12	7.20	10.35	24.45
Total current assets	**153.84**	**181.19**	**202.83**	**231.44**	**246.59**	**269.87**
TOTAL ASSETS	**260.64**	**345.29**	**368.19**	**390.78**	**406.48**	**441.53**
Shareholders'equity	**177.06**	**246.25**	**246.90**	**262.45**	**286.28**	**322.63**
Minorities	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Hybrid capital and other reserves	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Pension and other LT personnel accruals	0.00	0.00	0.00	0.00	0.00	0.00
Other LT provisions	3.49	2.40	1.00	1.00	1.00	1.00
Interest-bearing LT debts	1.76	2.14	0.87	0.40	0.20	0.00
Other LT liabilities	0.79	1.66	0.58	0.10	0.10	0.10
Total long-term liabilities	**2.55**	**3.81**	**1.45**	**0.50**	**0.30**	**0.10**
Interest-bearing ST debts	39.63	51.30	70.53	73.53	69.05	64.45
Other ST liabilities	37.90	41.53	48.30	53.31	49.85	53.34
Total short-term liabilities	**77.54**	**92.83**	**118.83**	**126.84**	**118.90**	**117.79**
TOTAL LIAB. , EQUITY	**260.64**	**345.29**	**368.19**	**390.78**	**406.48**	**441.53**

Cash Flow Statement	**2006**	**2007**	**2008**	**2009e**	**2010e**	**2011e**
(RAS,RON mn, 31/12)						
Cash flow from operating activities	38.36	27.19	16.30	-20.81	28.70	40.77
Cash flow from investing activities	-8.74	-11.18	-6.68	-10.82	-15.22	-17.06
Cash flow from financing activities	-6.39	-7.99	-4.18	-3.30	-10.33	-9.60
CHANGE IN CASH , CASH EQU.	**23.23**	**8.02**	**5.43**	**-34.92**	**3.15**	**14.11**

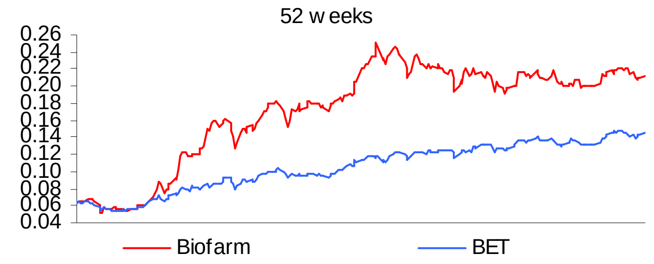
Margins & Ratios	**2006**	**2007**	**2008**	**2009e**	**2010e**	**2011e**
Sales growth	19.7%	17.2%	-5.9%	4.6%	7.4%	8.5%
EBITDA margin	23.1%	21.8%	17.2%	19.0%	15.8%	19.1%
EBIT margin	17.1%	18.0%	11.3%	13.1%	9.7%	13.3%
Net profit margin	14.4%	13.9%	4.7%	6.9%	6.8%	9.6%
ROE	17.6%	15.3%	4.3%	6.1%	6.2%	8.5%
ROCE	16.4%	15.0%	4.9%	6.5%	6.3%	8.4%
Equity ratio	67.9%	71.3%	67.1%	67.2%	70.4%	73.1%
Net debt	12.7	16.8	29.3	66.7	58.9	40.0
Working capital	76.1	87.9	83.7	104.3	127.4	151.8
Capital employed	194.1	267.1	277.8	330.3	346.3	363.7
Inventory turnover	2.3	2.7	2.2	1.6	1.3	1.4

Source: Company data, Erste Group estimates

Biofarm Hold

Raluca Ungureanu, +4021 311 27 54 raluca.ungureanu@bcr.ro

RON mn	2008	2009e	2010e	2011e
Net sales	65.1	68.4	75.2	83.5
EBITDA	18.6	18.6	19.0	23.4
EBIT	14.5	14.1	14.6	18.5
Net result after min.	-21.3	18.9	13.2	16.6
EPS (RON)	-0.02	0.02	0.01	0.02
CEPS (RON)	-0.02	0.02	0.02	0.02
BVPS (RON)	0.12	0.14	0.15	0.16
Div./share (RON)	0.00	0.00	0.00	0.00
EV/EBITDA (x)	2.7	10.1	9.4	7.0
P/E (x)	nm	12.2	17.5	13.9
P/CE (x)	-5.0	9.9	13.1	10.8
Dividend Yield	0.0%	0.0%	0.0%	0.0%



Performance	12M	6M	3M	1M
in RON	224.6%	3.4%	5.5%	5.0%
in EUR	241.6%	6.9%	11.4%	8.9%

Share price (RON)	0.21	Reuters	BIOF.BX	Free float	57.0%
Number of shares (mn)	1,094.9	Bloomberg	BIO RO	Shareholders	SIF Oltenia (17.0%)
Market capitalization (RON mn / EUR mn)	231 / 57	Div. Ex-date			SIF Banat Crisana (14%)
Enterprise value (RON mn / EUR mn)	188 / 46	**Target price**	**0.222**	Homepage:	www.biofarm.ro

Cautious market approach

- **We have slightly raised our target price for Biofarm to RON 0.222 (from RON 0.21), as result of including a lower risk-free rate (8%; previously 10%) in our DCF model for the detailed forecast period. We maintain our Hold recommendation, reflecting a rather cautious stance on the company, due to the payment constraints along the pharmaceutical chain and lower demand for OTC drugs, which represent the company's core business.**

- **Management continues its strategy of developing the sales force and has adopted a more cautious sales strategy, preferring to sell less than risk not recovering receivables, due to pharmacies going bankrupt. It is worth mentioning that payments for Rx drugs have not been made since July of last year, which has generated big financing issues for pharmacies, with many of them facing bankruptcy (particularly the smaller ones).**

- **We have revised our estimates for FY09 in order to account for the delay in implementing the clawback system, but also to capture the reversal of provisions that the company made in 2008 for the depreciation of its stock portfolio. Thus, we expect EBIT at RON 14.1mn for FY09 and net profit at RON 18.9mn, due to the estimated RON 6mn provision reversal. The changes in estimates for FY09 had only a marginal impact on the valuation.**

- **As no major events have occurred since our previous report, we did not revise our assumptions for the detailed forecast period (2010-14), except for the exchange rate development, which did not have a major impact on our estimates.**

Changes in forecast/outlook

We have revised our estimates for FY09 in order to reflect the results reported by the company for 3Q09, but also due to changes in some of our assumptions.

Results slightly better than expected in 3Q09

The company's 3Q09 results were broadly in line with our estimates. Thus, sales amounted to RON 16.7mn, which was 9% above our RON 15.04mn estimate. However, the effect of the low base must be considered when looking at the difference between the two numbers. EBIT was RON 3.6mn, some 1.1% below our estimate, whereas the RON 3.05mn net profit was 3.6% higher than our forecast.

4Q09 net sales to amount to RON 17.8mn

For the last quarter of 2009, we have adjusted by 7% the net sales forecast to RON 17.8mn, broadly assuming management's guidance that the company would rather sell less than risk not being paid, as many pharmacies (especially smaller ones) may face bankruptcy, due to the very long period for collecting receivables along the pharma chain (300 days or more).

We adjusted 4Q09 EBIT to RON 2.9mn (from RON 3.5mn)

We have also made some adjustments on the operating expenses side, as a result of the clawback system not being implemented yet, while we have assumed the company recording a 6% tax on sales of Rx drugs in 4Q09. Due to the company not being largely exposed to the drug categories addressed by the clawback system, the impact of this tax will be limited (compared to peer Antibiotice, for instance). The joint effect of the above changes in assumptions led to EBIT of RON 2.9mn for 4Q09, slightly below the previous estimate of RON 3.5mn.

RON 6mn provision reversal to boost net profit in 2009 to RON 18.9mn

The biggest change in our estimates for FY09 occurred on the financial result side. In our previous report, we wrote that a partial reversal of the provisions made by the company in 2008 for the depreciation of its stock portfolio is likely. Now, we have incorporated an estimate of this provision reversal of some RON 6mn. This is expected to boost the company's net profit in 2009 to RON 18.9mn - a spectacular level for the company. Investors must be aware of the fact that this is only a partial reversal of the RON 35.14mn provision made in 2008. Management's strategy for the stock portfolio is to wait until the initial investment (EUR 10mn) can be recovered. However, our expectation is that the remarkable net profit will fuel positive market sentiment after the announcement of the preliminary financial results in February. In spite of this, we remain cautious on this stock, considering the challenging economic environment.

Change in estimates

RAS (RON, mn)	2009e Now	Before	*Change*
Net sales	68.4	68.4	*0.0%*
Total revenues	68.7	69.0	*-0.5%*
Material costs	19.9	20.9	*-4.6%*
Personnel costs	13.4	13.8	*-3.2%*
Other operating expenses	17.1	17.8	*-3.5%*
EBITDA	18.6	17.1	*8.7%*
EBIT	14.1	12.9	*9.8%*
Financial result	8.4	0.2	*n.m.*
Net income	18.9	11.0	*71.9%*

Source: Erste Group Research

As no major changes have occurred since our previous report, we maintain our estimates for the period 2010-14, except for the local currency development, which we have updated, albeit without a significant impact.

Expected 10% increase in sales this year

To summarize, we expect sales to advance this year by some 10%, on the back of a recovery in volume terms by the end of the year and a slight increase in prices. The company has the competitive advantage of traditional brands and lower prices, which provides room for price increases. Up to the end of the detailed forecast period, we expect sales to increase at an annual rate of 11-13%, mainly on the back of higher quantities sold. Broadly assuming management's guidance, we have estimated the EBIT margin falling in 2010, due to higher marketing and sales expenses, as well as the impact of the clawback system. Given the patchy guidance regarding the way that the clawback system is to work, we have assumed that Biofarm will be charged a 6% tax on sales of reimbursed drugs.

EBIT margin to stabilize at 22-23% starting in 2011

Starting in 2011, we expect the EBIT margin to stabilize at 22-23%. The two main reasons underlying our forecast are: i) the main shareholders plan to exit the company in a few years; thus, management is highly motivated to make the figures look good; and ii) management has room to increase prices, considering competitors' substantially higher product prices.

Valuation summary

We have updated our 5-year DCF model employed for the valuation of the company in order to incorporate the changes that have occurred in terms of the risk-free rate, while keeping the other assumptions unchanged. Thus, the main assumptions underlying our analysis are:
- Risk-free rate at 8% for the detailed forecast period (from 10% previously), due to lower government bond yields.
- Beta at 1.
- Equity ratio at 90%.

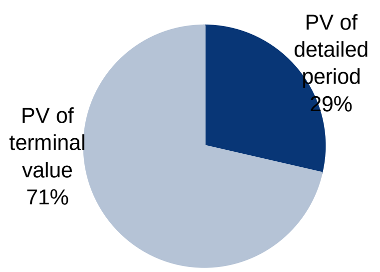
WACC calculation

	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Risk free rate	8.0%	8.0%	8.0%	8.0%	8.0%	6.0%
Equity risk premium	7.2%	7.2%	7.2%	7.2%	7.2%	6.7%
Beta	1.0	1.0	1.0	1.0	1.0	1.0
Cost of equity	**15.2%**	**15.2%**	**15.2%**	**15.2%**	**15.2%**	**12.7%**
Cost of debt	10.5%	10.5%	10.5%	10.5%	10.5%	8.5%
Effective tax rate	18.0%	18.0%	18.0%	18.0%	18.0%	16.0%
After-tax cost of debt	**8.6%**	**8.6%**	**8.6%**	**8.6%**	**8.6%**	**7.1%**
Equity weight	90%	90%	90%	90%	90%	90%
WACC	**14.5%**	**14.5%**	**14.5%**	**14.5%**	**14.5%**	**12.1%**

DCF valuation

(RON mn)	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Sales growth	*10.0%*	*11.0%*	*13.0%*	*13.0%*	*9.0%*	*4.5%*
EBIT	14.6	18.5	21.0	24.7	27.4	28.9
EBIT margin	*19.0%*	*22.0%*	*22.0%*	*22.9%*	*23.3%*	*23.5%*
Tax rate	*18.0%*	*18.0%*	*18.0%*	*18.0%*	*18.0%*	*16.0%*
Taxes on EBIT	-2.6	-3.3	-3.8	-4.4	-4.9	-4.6
NOPLAT	**11.9**	**15.2**	**17.2**	**20.2**	**22.5**	**24.2**
+ Depreciation	4.4	4.9	5.3	5.7	6.0	6.5
Capital expenditures / Depreciation	*149.5%*	*132.8%*	*121.0%*	*109.5%*	*103.2%*	*100.0%*
+/- Change in working capital	-1.3	-1.3	-1.7	-1.9	-1.5	-0.8
Chg. working capital / chg. Sales	*-16.8%*	*-17.3%*	*-15.6%*	*-15.1%*	*-15.3%*	*-15.0%*
- Capital expenditures	-6.7	-6.5	-6.4	-6.2	-6.2	-6.5
Free cash flow to the firm	**8.4**	**12.3**	**14.4**	**17.8**	**20.8**	**23.4**
Terminal value growth						*2.0%*
Terminal value						236.8
Discounted free cash flow - Dec 31 2009	7.3	9.4	9.6	10.4	10.6	118.0
Enterprise value - Dec 31 2009	**165.1**					
Minorities	0.0					
Non-operating assets	0.0					
Net debt	-43.3					
Other adjustments	0.0					
Equity value - Dec 31 2009	**208.4**					
Number of shares outstanding (mn)	1,094.9					
Cost of equity	15.2%					
12M target price per share (RON)	**0.222**					
Current share price (RON)	0.211					
Up/Downside	*5.1%*					

Enterprise value breakdown



Sensitivity (per share)

	Terminal value EBIT margin				
WACC	22.5%	23.0%	23.5%	24.0%	24.5%
11.1%	0.229	0.233	0.236	0.239	0.242
11.6%	0.223	0.225	0.228	0.231	0.234
12.1%	0.216	0.219	**0.222**	0.225	0.227
12.6%	0.211	0.213	0.216	0.219	0.221
13.1%	0.205	0.208	0.211	0.213	0.216

	Terminal value growth				
WACC	1.0%	1.5%	2.0%	2.5%	3.0%
11.1%	0.222	0.228	0.236	0.244	0.253
11.6%	0.216	0.222	0.228	0.236	0.244
12.1%	0.211	0.216	**0.222**	0.228	0.236
12.6%	0.206	0.211	0.216	0.222	0.228
13.1%	0.201	0.206	0.211	0.216	0.222

Source: Erste Group Research

Income Statement	2006	2007	2008	2009e	2010e	2011e
(RAS, RON mn, 31/12)	31/12/2006	31/12/2007	31/12/2008	31/12/2009	31/12/2010	31/12/2011
Net sales	**57.83**	**62.34**	**65.10**	**68.36**	**75.19**	**83.47**
Invent. changes + capitalized costs	-1.09	0.06	1.11	0.36	1.52	0.95
Total revenues	**56.74**	**62.41**	**66.21**	**68.71**	**76.71**	**84.42**
Other operating revenues	0.17	0.29	0.14	0.34	0.55	0.62
Material costs	-16.16	-17.00	-19.64	-19.95	-22.08	-24.51
Personnel costs	-10.87	-11.89	-13.11	-13.38	-14.42	-14.85
Other operating expenses	-11.60	-14.26	-15.00	-17.14	-21.77	-22.24
EBITDA	**18.28**	**19.54**	**18.60**	**18.59**	**19.00**	**23.44**
Depreciation/amortization	-3.61	-4.21	-4.05	-4.45	-4.45	-4.89
EBIT	**14.68**	**15.33**	**14.55**	**14.15**	**14.55**	**18.54**
Financial result	0.30	0.64	-33.42	8.40	1.18	1.21
Extraordinary result	0.00	0.00	0.00	0.00	0.00	0.00
EBT	**14.98**	**15.97**	**-18.87**	**22.55**	**15.73**	**19.75**
Income taxes	-2.26	-2.46	-2.44	-3.61	-2.52	-3.16
Result from discontinued operations	0.00	0.00	0.00	0.00	0.00	0.00
Minorities and cost of hybrid capital	0.00	0.00	0.00	0.00	0.00	0.00
Net result after minorities	**12.72**	**13.51**	**-21.31**	**18.94**	**13.21**	**16.59**

Balance Sheet	2006	2007	2008	2009e	2010e	2011e
(RAS, RON mn, 31/12)						
Intangible assets	0.36	0.38	1.33	1.68	1.99	2.26
Tangible assets	40.80	69.12	70.12	71.48	73.37	74.71
Financial assets	0.00	40.65	6.97	13.03	13.03	13.03
Total fixed assets	**41.16**	**110.14**	**78.43**	**86.19**	**88.40**	**90.00**
Inventories	7.47	8.55	12.67	13.11	14.01	15.09
Receivables and other current assets	12.85	17.39	19.10	22.47	24.31	26.53
Other assets	0.14	0.17	0.27	0.00	0.00	0.00
Cash and cash equivalents	24.37	30.03	36.45	43.88	52.73	65.98
Total current assets	**44.82**	**56.14**	**68.49**	**79.46**	**91.05**	**107.60**
TOTAL ASSETS	**85.98**	**166.29**	**146.92**	**165.66**	**179.44**	**197.60**
Shareholders'equity	**70.53**	**151.02**	**129.71**	**148.65**	**161.87**	**178.46**
Minorities	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Hybrid capital and other reserves	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Pension and other LT personnel accruals	0.00	0.00	0.00	0.00	0.00	0.00
Other LT provisions	1.82	2.10	2.12	2.05	2.05	2.05
Interest-bearing LT debts	1.41	1.09	0.24	0.26	0.05	0.00
Other LT liabilities	0.71	0.42	0.79	0.65	0.64	0.62
Total long-term liabilities	**2.12**	**1.51**	**1.03**	**0.91**	**0.69**	**0.62**
Interest-bearing ST debts	0.63	0.87	0.96	0.37	0.00	0.00
Other ST liabilities	10.87	10.79	13.11	13.67	14.84	16.47
Total short-term liabilities	**11.50**	**11.66**	**14.07**	**14.04**	**14.84**	**16.47**
TOTAL LIAB. , EQUITY	**85.98**	**166.29**	**146.93**	**165.66**	**179.44**	**197.60**

Cash Flow Statement	2006	2007	2008	2009e	2010e	2011e
(RAS,RON mn, 31/12)						
Cash flow from operating activities	13.15	12.65	11.76	11.58	15.31	19.15
Cash flow from investing activities	-5.22	-42.86	-3.28	-2.73	-5.45	-5.30
Cash flow from financing activities	-2.80	35.86	-2.07	-1.42	-1.00	-0.60
CHANGE IN CASH , CASH EQU.	**5.12**	**5.66**	**6.42**	**7.43**	**8.85**	**13.25**

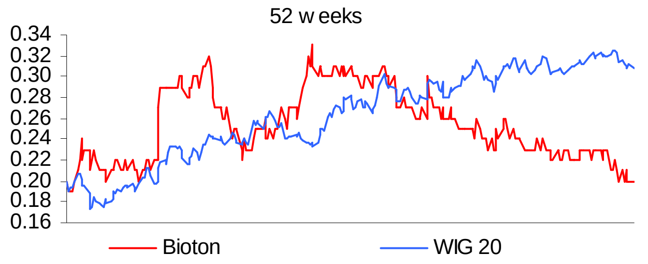
Margins & Ratios	2006	2007	2008	2009e	2010e	2011e
Sales growth	14.6%	7.8%	4.4%	5.0%	10.0%	11.0%
EBITDA margin	32.2%	31.3%	28.1%	27.1%	24.8%	27.8%
EBIT margin	25.9%	24.6%	22.0%	20.6%	19.0%	22.0%
Net profit margin	22.4%	21.7%	-32.2%	27.6%	17.2%	19.7%
ROE	19.9%	12.2%	-15.2%	13.6%	8.5%	9.8%
ROCE	27.0%	14.5%	-20.8%	16.1%	11.3%	13.9%
Equity ratio	82.0%	90.8%	88.3%	89.7%	90.2%	90.3%
Net debt	-22.3	-28.1	-35.2	-43.3	-52.7	-66.0
Working capital	33.2	44.3	54.1	65.4	76.2	91.1
Capital employed	50.7	125.5	97.4	108.1	111.9	115.2
Inventory turnover	1.9	1.9	1.6	1.4	1.5	1.5

Source: Company data, Erste Group estimates

Bioton Hold

Vladimira Urbankova, MBA +43 50100 17343 vladimira.urbankova@erstegroup.com

PLN mn	2008	2009e	2010e	2011e
Net sales	293.5	290.3	450.4	416.6
EBITDA	-47.8	-45.8	154.0	104.1
EBIT	-71.5	-74.6	123.8	72.4
Net result after min.	-218.9	-75.3	94.1	48.0
EPS (PLN)	-0.07	-0.01	0.02	0.01
CEPS (PLN)	-0.07	-0.01	0.02	0.02
BVPS (PLN)	0.36	0.27	0.27	0.28
Div./share (PLN)	0.00	0.00	0.00	0.00
EV/EBITDA (x)	-24.6	-27.1	7.5	10.7
P/E (x)	nm	nm	11.2	22.0
P/CE (x)	-3.1	-22.8	8.5	13.3
Dividend Yield	0.0%	0.0%	0.0%	0.0%



Performance	12M	6M	3M	1M
in PLN	0.0%	-33.3%	-13.0%	-13.0%
in EUR	11.7%	-30.8%	-7.3%	-10.5%

Share price (PLN)	0.20	Reuters	BOTN.WA	Free float	66.5%
Number of shares (mn)	5,290.4	Bloomberg	BIO PW	Shareholders	Prokom Investment (28.7%)
Market capitalization (PLN mn / EUR mn)	1,058 / 265	Div. Ex-date			IBA (4.8%)
Enterprise value (PLN mn / EUR mn)	1,239 / 309	**Target price**	**0.21**	Homepage:	www.bioton.pl

Polpharma cooperation / merger deal to brighten outlook

- **The news flow from Bioton remains mixed. On one hand, the cooperation (possibly ending in a merger) deal with Polpharma, including the sale of the antibiotics segment and disposal of the Italian subsidiaries, could unlock Bioton's potential, allowing it to concentrate its resources on its core insulin business and solidify its prospects in the biotech field. On the other hand, the restructuring process is slower than originally assumed, with postponements marking not only the Bioton Wostok sell-off, but also the important start of insulin sales in China (in cooperation with Bayer). Our revised 12M DCF-derived target price (including the newly introduced 10% risk–related discount) arrives at PLN 0.21 per share (vs. the earlier target of PLN 0.26). With the delays pointing to persisting risks, but with the Polpharma deal to possibly brighten the outlook, we stick to our Hold recommendation on the stock.**

- **We incorporated into our model 1) the significantly greater than originally assumed burden of the restructuring on the operating result in 2009; 2) the more subdued sales tempo and meager gross profitability in 3Q09; 3) the delays in the Bioton Wostok disposal, along with postponements of the insulin market launch in China. Here, we want to reiterate that, given the lack of information, our projections currently do not include any possible future restructuring steps (most importantly, the sale of the Italian operations and/or the antibiotics unit). All told, we cut our sales target for 2009 to PLN 290.3mn (down 6.3% vs. our earlier target) and we revise our bottom line forecast to a net loss of PLN 75.3mn (vs. the earlier targeted net loss of PLN 54.7mn).**

- **We expect the 4Q09 results (scheduled for release on March 1, 2010) to further demonstrate the company's restructuring pains. Reflecting the year-earlier low comparative base, we forecast Bioton's sales advancing by about 21% y/y to PLN 73.0mn. While we continue to assume forex and investment revaluation losses plaguing the financial result, the effect should be less detrimental y/y. The bottom line is expected to stay in red territory in 4Q09 at a loss of some PLN 25.2mn, a much better figure than the year-earlier net loss of PLN 181.7mn (which was weighed down by huge financial losses related to Bioton Wostok write-offs).**

Changes in forecast/outlook

Reflecting sluggish 1-3Q09, we reduce our 2009 sales target to PLN 290.3mn

The 1-3Q09 report provided further evidence of the distorting impact of one-off items in the comparative base on the company's top line progress. While the company benefited from the first-time consolidation effect (Pharmatex, Fisiopharma and MJ Bioton Life Sciences) on its sales, the impact was not sufficient to fully offset the missing support from the one-off income related to the sale of product rights recorded in the year-earlier period (PLN 30.7mn). Bioton's sales slipped by 6.1% y/y to PLN 218.8mn in 1-3Q09, lagging some 4.9% behind our estimate. While we believe that the relatively low comparative base in the last quarter of the year offers some running space, we keep our conservative stance and trim our sales forecast for 2009 from PLN 309.7mn to PLN 290.3mn. Insulin sales remain the backbone of Bioton's strategy. For 2009, they are anticipated to deliver a substantial chunk of the company's sales. Nevertheless, the sales growth in this segment was dampened in 2009, due not least to the subdued performance in Russia. Not only was the company's tender-driven insulin business in Russia highly irregular, with practically no Russian insulin sales recorded in some quarters, but exports to the Russian pharmaceutical market suffered from ruble depreciation in 2009. With 1-3Q09 data pointing to persisting weakness, we slightly decrease our forecasts, anticipating Bioton's sales in Russia at a mere PLN 10mn (down from the earlier projected USD 3.6m, or PLN 11.4mn) in 2009. In total, we project Bioton's 2009 insulin sales at PLN 115mn, out of which the domestic market is expected to deliver around PLN 71mn. Going forward, while we continue to believe that Russia represents an attractive market for insulin manufacturers, Bioton's fortunes there will largely depend on the successful closing of the disposal of its stake in its Russian JV, Bioton Wostok, including finding a suitable cooperation partner for insulin sales and distribution.

While a lot of uncertainties remain here and the outlook is rather opaque, Bioton's insulin exports should get a strong impetus from the cooperation contract signed in June last year with Germany's Bayer. Based on the contract (valid until 2015), Bioton will supply its partner with insulin for the Chinese market. For the exclusive right to market and distribute insulin produced by Bioton under the trade name SciLin in China, Bayer is obliged to make an upfront payment of EUR 31mn. According to Bioton, the total value of revenues related to the Bayer contract over the 15 years is anticipated in the range of USD 1.5bn to USD 2bn. Unfortunately, this project has already registered its first delays, with the first insulin deliveries now anticipated for September 2010 (instead of mid-2010). We remain on the conservative side and, despite the envisaged positive impact from the introduction of an insulin pen on Bioton's home market, we lower our assumptions. In total, we project Bioton's total insulin sales slightly exceeding PLN 135mn (vs. the earlier forecast of PLN 144mn) in 2010, out of which around PLN 8mn (down from the earlier assumed PLN 40mn) is to be attributable to the contract with Bayer. Here we want to reiterate that, based on the latest information from the company, only the first tranche (EUR 6mn) out of the EUR 31.0mn milestone payment from the Bayer contract is likely to be recorded under restricted cash in 2009 and the milestone payment will not affect the company's P&L statement in 2009. Hence, we stick to our earlier assumption that the milestone payment will give a lift to Bioton's top line only in 2010.

As consolidating the two Italian companies (Pharmatex Italia and Fisiopharma) started only in 2Q08, 2009 (as the first full year of consolidation) should see a positive impact from these acquisitions. Nevertheless, their contribution is anticipated at around EUR 11mn, somewhat below the original goal (EUR 14-15mn). Our 2009 forecast for antibiotics sales on the domestic market remains at PLN 66mn. According to the letter of intent signed between Polpharma and Bioton, the antibiotics segment is likely to disappear from Bioton's business portfolio, with Polpharma taking it over. Nevertheless, the timing of the closing, as well as other details (including the final price tag), are not known yet. Hence, we leave our forecasts unchanged. As before, reflecting the persisting silence on the Biferonex front, we omit the project from our projections. We cut our 2009 sales forecast from PLN 309.7mn to PLN 290.3mn, corresponding to a 1.1% y/y drop. Reflecting in part the recently announced delays in launching insulin in China, as well as the lower comparative base, we decrease our 2010 top line target to PLN 450.4mn (down from the PLN 471.1mn projected earlier).

Climbing restructuring costs drag EBIT deeply into red; we cut our 2009 EBIT target to loss of PLN 74.6mn

The streamlining of operations, including the disposal of certain assets, keeps its priority on Bioton's restructuring agenda. Nevertheless, the plans are only gradually taking a more concrete shape and their materialization will undoubtedly take some time. The first deal - the sale of Bioton's stake in Bioton Wostok – has been marked by permanent delays. Originally, it was expected to be finalized in June 2009. Despite progress in autumn, the transaction was not completed before the end of last year. In October 2009, Bioton announced that the French pharmaceutical company Sanofi-Aventis bought a 74% stake in Bioton Wostok from Bioton and Russian investor Siergiej W. Dokuczajew. Bioton will obtain EUR 28mn for its 38% stake in Bioton Wostok, while Dokuczajew sold a 36% stake for an undisclosed sum. Bioton anticipates receiving an additional USD 1.5-2.5mn (after the final accounting for working capital is done) after the completion of the transaction. The closing of the deal is subject to approval from the Russian competition authorities. In line with the company's guidance, we assume that (after a big cleanup of the 2008 balance sheet) the transaction will be broadly neutral for the consolidated P&L statement. (Reclassification of Bioton Wostok as an asset for sale resulted in diminishing losses from the share of equities accounted for with the equity method starting from 2Q09.)

Backed by Bayer deal milestones, first restructuring gains, 2010 should see turnaround

Another bold restructuring move happened in November 2009, when Bioton inked a letter of intent that could result in the merger of Bioton with Polpharma. The letter of intent refers to cooperation between Bioton and Polpharma in respect to (1) the possibility of a merger with Polpharma; (2) the potential purchase by Polpharma of the antibiotics production unit of Bioton; and (3) the potential purchase by Polpharma of the Italian drug producing subsidiaries of the company. The company should obtain some PLN 90-110mn from the sale of its antibiotics segment, with the proceeds to be used on developing high-margin biotech products and enabling the company to fully focus on developing insulin sales and production, as well as other biotech products. The planned sale of the Italian subsidiaries should accelerate the restructuring of Bioton. The company announced that a study of the merger with Polpharma will be prepared by December 15, 2009; by February 28, 2010, both sides will decide on the merger possibility and its basic parameters; by August 30, 2010, the merger plan could be signed. The contract regarding the sale of the antibiotics segment and the Italian units is expected to be inked by end-February 2010. Nonetheless, the only information market participants have received so far about the progress in the above-mentioned cooperation with Polpharma was the confirmation that Polpharma in December 2009 sought approval for the acquisition of part of Bioton's assets. A study of the possible merger has not been published yet. At the moment, we lack information about the above-mentioned potential transactions (including their timing and likely proceeds), so we continue to stick to our basic scenario for Bioton, keeping its status quo in our forecasts. The only deal reflected at least partly in our assumptions is the disposal of Bioton Wostok.

Change in estimates

Consolidated, IFRS	2009e			2010e		
(PLN, mn)	Now	Before	*Change*	Now	Before	*Change*
Net sales	**290.3**	**309.7**	***-6.3%***	**450.4**	**471.1**	***-4.4%***
Costs of goods sold	175.8	183.2	*-4.1%*	177.3	185.4	*-4.4%*
Gross profit	**114.5**	**126.6**	***-9.5%***	**273.1**	**285.7**	***-4.4%***
Sales & marketing exp.	50.5	53.9	*-6.3%*	56.3	61.2	*-8.1%*
General & admin. exp.	102.3	88.3	*15.9%*	76.6	75.4	*1.6%*
Other operating income	27.6	21.2	*30.0%*	15.1	15.1	*0.1%*
Other operating exp.	63.9	63.5	*0.6%*	31.5	33.0	*-4.4%*
Operating profit	**-74.6**	**-57.9**	***28.9%***	**123.8**	**131.2**	***-5.6%***
Financial result	-13.1	-12.2	*6.6%*	-11.9	-11.0	*8.4%*
Pre-tax profit	-87.7	-70.1	*25.0%*	111.9	120.2	*-6.9%*
Income taxes	-8.8	-13.3	*-34.2%*	21.3	22.8	*-6.9%*
Minority interest	3.6	2.1	*74.0%*	3.4	2.0	*74.0%*
Net income	**-75.3**	**-54.7**	***37.5%***	**94.1**	**99.3**	***-5.3%***
Gross margin	39.4%	40.9%		60.6%	60.6%	
EBIT margin	-25.7%	-18.7%		27.5%	27.8%	
Net margin	-25.9%	-17.7%		20.9%	21.1%	

Source: Erste Group Research

Gross profitability remained subdued in 1-3Q09 (with a gross margin of 38.6%), given the deterioration in 3Q09 (to a gross margin of 36.7%, from the 2Q09 level of 42.4%), lagging behind our expectations. Consequently, we are forced to make a downward adjustment in our 2009 gross margin target, from 40.9% to 39.4%. As before, we envisage the Bayer deal milestone payments, along with the first restructuring gains, as the main driver for significant improvement in the 2010 gross margin. We continue to believe that our gross margin target of 60.6% is achievable. Most importantly, 1-3Q09 operating expenses were far higher than we had assumed, due in particular to climbing restructuring costs (including further R&D project write-offs) and elevated G&A expenses, prompting us to adjust our operating cost assumptions for 2009. According to the company, the 1-3Q09 restructuring bill was as follows: PLN 15.5mn represented direct restructuring costs in Poland and at SciGen, PLN 5.1mn was expenses related to the implementation of a new strategy (namely preparation of contracts with Bayer in China, disposal of Bioton Wostok, etc.) and finally PLN 21.7mn was asset write-offs. Sales and marketing spending remained the only item where the company continued with rather modest spending in 3Q09. Hence, we opt for a minor cut to our original assumptions for 2009 and envisage sales and marketing costs at around PLN 50.5mn (vs. the earlier projected PLN 53.9mn). Although the administrative and general costs' burden got a bit easier q/q in 3Q, the 1-3Q09 pace was still well above expectations, prompting us to raise our 2009 forecast from PLN 88.3mn to PLN 102.3mn. Hampered by asset (including R&D project) write-offs, other operating costs skyrocketed to PLN 48.2mn in 1-3Q09, out of which the third quarter added PLN 8.6mn. Severance payments linked to personnel cuts at the Polish operations were reflected in separately reported restructuring costs amounting to PLN 6.2mn in 1-3Q09 (with all costs actually incurred in 2Q09).

In summary, reflecting the hampering impact of the y/y hike in G&A costs and the restructuring burden in 1-3Q09, our new 2009 operating line target arrives at a loss of PLN 74.6mn (down from the PLN 57.9mn operating loss projected earlier), translating into an operating profit margin of a negative 25.7% (down from the previous -18.7% forecast). For 2010, we continue to project a relatively significant increase in sales and marketing costs, mirroring more intense marketing efforts in the core insulin business. Cost containment measures in the area of general and administrative expenses remain a target for management. Nevertheless, the progress here will undoubtedly depend on the pace of restructuring – namely, the disposal of foreign operations. However, the worse than anticipated 1-3Q09 figures temper optimism here. Consequently, we raise our general and administrative cost forecast from PLN 75.4mn to PLN 76.6mn, or around 17% of sales in 2010. All told, bolstered by a milestone payment-attributable cushion, we still believe that Bioton is heading for a turnaround in its operating profitability in 2010 and project the EBIT margin soaring to 27.5%. Given the bigger than earlier anticipated restructuring blow to the 2009 numbers, we set a new 2010 operating profit target of PLN 123.8mn, somewhat below our previous estimate of PLN 131.2mn.

3Q09 financial result only marginally behind expectations; despite lower financial result burden, bottom line to stay in red in 2009

In line with our earlier expectations, the company's financial result stayed in black territory after the first nine months of 2009, although 3Q09 switched back to red territory (to a loss of PLN 8.5mn). Apart from the gain (of PLN 8.6mn) on the disposal of Bioton's stake in HTL-Strefa, the positive forex result and reversal of previous write-offs of financial assets played major roles in the positive nine-month balance. In addition, due to the reclassification of Bioton Wostok under assets for sale, the company's losses at foreign subsidiaries (amounting to PLN 16mn in 1Q09) stopped harming the company's 2009 financial result. Although part of the financial expenses remain difficult to predict (in particular, forex and possible investment revaluation related losses), the improving financial position of the company (due not least to the waves of capital injections) lead us to believe that the FY09 financial result is poised to turn for the better, in particular compared to the disappointing 2008 performance. Nevertheless, the delays in the disposal of Bioton Wostok represent a negative factor compromising the outlook, as the related proceeds were intended to lower indebtedness. In the meantime, financing costs have become higher (compared to the original management forecasts projecting a cut in Bioton's debt to PLN 164mn by end-2009). Nonetheless, we believe that our 2009 forecast of a financial loss of PLN 13.1mn is achievable. All told, although the operating line sank deeper into the red in the course of 2009 and 4Q09 is unlikely to rescue the show, we think that the net loss should shrink significantly y/y. Incorporating the worse than envisaged EBIT, we revise our net loss forecast from PLN 54.7mn to PLN 75.3mn in 2009 (this compares to the 2008 net loss of PLN 218.9mn). For 2010, we remain cautiously optimistic and, assuming support from milestone payments, we project net profit advancing to PLN 94.1mn.

4Q09 results preview

IFRS consolidated	4Q2009e	4Q2008	y/y	1-4Q2009e	1-4Q2008	y/y
Total sales (PLN 000)	73,041	60,403	*20.9%*	290,284	293,517	*-1.1%*
Operating profit (PLN 000)	-19,366	-90,806	*-78.7%*	-74,605	-71,487	*4.4%*
Net income (PLN 000)	-25,158	-181,736	*-86.2%*	-75,294	-218,892	*-65.6%*
Operating margin	*-26.5%*	*-150.3%*		*-25.7%*	*-24.4%*	
Net margin	*-34.4%*	*-300.9%*		*-25.9%*	*-74.6%*	

Source: Erste Group Research

Bioton is scheduled to announce its 4Q09 results on March 1, 2010. We expect a 4Q09 net loss of PLN 25.2mn on sales of PLN 73.0mn (consolidated and according to IFRS standards), translating into a 2009 net loss of PLN 75.3mn on sales of PLN 290.3mn. We forecast Bioton's sales up 21% y/y to PLN 73.0mn in 4Q09, with the low comparative base playing in favor of the company's y/y progress. Nonetheless, as the consolidation of the two Italian companies and MJ Bioton Life Sciences will largely compensate for the absence of a one-off payment related boost, we expect Bioton's sales slipping by 1.1% y/y on a cumulative basis in 2009. The subdued profitability parameters of the newly consolidated companies and (most importantly) the mounting restructuring costs are expected to continue to bite into the company's profitability margins. We forecast the operating line staying in red territory in 4Q09, with the operating loss narrowing to PLN 19.4mn in 4Q09 (vs. the year-earlier operating loss of PLN 90.8mn). For the full year, our operating loss target arrives at PLN 74.6mn. The y/y dramatically improving financial result bodes well for a shrinking of the 4Q09 bottom line loss as well. We envisage the net loss decreasing to PLN 75.3mn in 2009; for 4Q09 alone, we project a net loss of PLN 25.2mn, a much better figure than the year-earlier loss of PLN 181.7mn (which was weighed down by huge financial losses related to Bioton Wostok write-offs).

Valuation Summary

We revise our 12-month target price to PLN 0.21 and stick to Hold

We stick to the parameters of our DCF model presented in our sector report from November 2009 (factoring in the risk-free rate of 6.0%) and the unified methodology for setting the equity risk premium (applying the equity risk premium for 2010-14 of 6.0% and 5.0% for perpetuity). Incorporating the latest forecast changes (including further postponements in asset disposals and the Chinese market insulin launch) into our model, we arrive at a 12-month target value of PLN 0.23 per share. Nevertheless, as the company's outlook remains opaque, we decided to introduce a risk-related discount of 10% to our DCF-derived target price, yielding a new target price of PLN 0.21 (down from the PLN 0.26 per share targeted earlier). Bioton's share price development in 2009 demonstrated a relatively high degree of resilience to the weak 2009 interim reports. Nevertheless, the stock was not completely immune to the mounting uncertainties, with permanent postponements in execution of strategic plans. The frequent top management changes (with CEO Janus Guy leaving the company just a few months after presenting the applauded strategy and the company appointing its third CFO within the past year) added to the investor worries. Furthermore, the repeated capital injections, while demonstrating the commitment of key shareholders and their trust in Bioton's turnaround, brought dilutive effects for minority shareholders in 2009. Hence, it was not surprising to see Bioton as the laggard, ending as the only stock in the CEE pharma universe with a negative share price performance in 2009. The start to 2010 was not promising either, with the reported delays in the Polpharma deal and insulin introduction in China dragging the stock price down further. The news flow around the crucial Polpharma cooperation/merger deal remains of ultimate importance for the business outlook as well as stock prospects going forward. We believe that the strengthened focus on the insulin niche and further product portfolio streamlining, including a thorough review of activities abroad and asset disposals, would benefit the company, boding well for its turnaround. Hence, these deserve to be carefully watched by market participants. Should the news flow related to the restructuring regain momentum, the positive sentiment would send the stock back on an appreciation path. Our revised 12-month target price of PLN 0.21 per share suggests that, as long as the clouds over Bioton's future do not dissipate, the current stock price offers only limited upside potential. With the Polpharma cooperation deal impact still difficult to incorporate into our Bioton forecasts, we leave our Hold recommendation on the stock unchanged.

Restructuring related news flow remains decisive factor for Bioton's share price

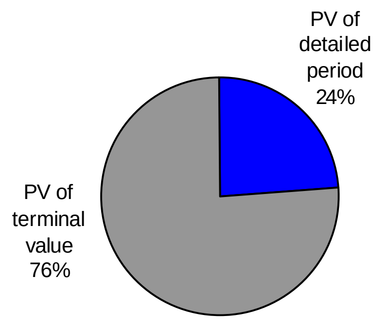
WACC calculation

	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Risk free rate	6.0%	6.0%	6.0%	6.0%	6.0%	5.0%
Equity risk premium	6.0%	6.0%	6.0%	6.0%	6.0%	5.0%
Beta	0.8	0.8	0.8	0.8	0.8	1.0
Cost of equity	**11.0%**	**11.0%**	**11.0%**	**11.0%**	**11.0%**	**10.0%**
Cost of debt	7.5%	7.5%	7.5%	7.5%	7.5%	6.5%
Effective tax rate	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%
After-tax cost of debt	**6.1%**	**6.1%**	**6.1%**	**6.1%**	**6.1%**	**5.3%**
Equity weight	89%	89%	89%	89%	89%	90%
WACC	**10.5%**	**10.5%**	**10.5%**	**10.5%**	**10.5%**	**9.5%**

DCF valuation

(PLN mn)	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Sales growth	*55.2%*	*-7.5%*	*21.4%*	*13.9%*	*11.6%*	*6.0%*
EBIT	123.8	72.4	91.0	113.1	131.8	129.4
EBIT margin	*27.5%*	*17.4%*	*18.0%*	*19.7%*	*20.5%*	*19.0%*
Tax rate	*19.0%*	*19.0%*	*19.0%*	*19.0%*	*19.0%*	*19.0%*
Taxes on EBIT	-23.5	-13.8	-17.3	-21.5	-25.0	-24.6
NOPLAT	**100.3**	**58.6**	**73.7**	**91.6**	**106.7**	**104.8**
+ Depreciation	30.1	31.7	33.4	35.3	37.4	37.4
Capital expenditures / Depreciation	*93.5%*	*95.8%*	*99.7%*	*99.7%*	*99.8%*	*100.0%*
+/- Change in working capital	-10.1	-6.6	-11.0	-9.2	-9.9	-5.8
Chg. working capital / chg. Sales	*-6.3%*	*19.5%*	*-12.4%*	*-13.2%*	*-14.8%*	*-15.0%*
- Capital expenditures	-28.2	-30.3	-33.3	-35.2	-37.4	-37.4
Free cash flow to the firm	**92.1**	**53.4**	**62.8**	**82.5**	**96.9**	**99.1**
Terminal value growth						*3.0%*
Terminal value						1,563.9
Discount factor	*0.91*	*0.82*	*0.74*	*0.67*	*0.61*	*0.55*
Discounted free cash flow - Dec 31 2009	83.4	43.7	46.6	55.4	58.9	922.9
Enterprise value - Dec 31 2009	**1,210.9**					
Minorities	66.0					
Non-operating assets	0.0					
Net debt	115.1					
Other adjustments	0.0					
Equity value - Dec 31 2009	**1,029.8**					
Number of shares outstanding (mn)	5,290.4					
Cost of equity	11.0%					
12M target price per share (PLN)	**0.23**					
- risk related discount	10.0%					
12M target price per share (PLN)	**0.21**					
Current share price (PLN)	0.20					
Up/Downside	*3%*					

Enterprise value breakdown



Sensitivity (per share)

	Terminal value EBIT margin				
WACC	18.0%	18.5%	19.0%	19.5%	20.0%
8.5%	0.23	0.23	0.24	0.25	0.25
9.0%	0.21	0.22	0.22	0.23	0.23
9.5%	0.20	0.20	**0.21**	0.21	0.22
10.0%	0.18	0.19	0.19	0.20	0.20
10.5%	0.17	0.18	0.18	0.19	0.19

	Terminal value growth				
WACC	2.0%	2.5%	3.0%	3.5%	4.0%
8.5%	0.21	0.22	0.24	0.26	0.29
9.0%	0.19	0.21	0.22	0.24	0.26
9.5%	0.18	0.19	**0.21**	0.22	0.24
10.0%	0.17	0.18	0.19	0.21	0.22
10.5%	0.16	0.17	0.18	0.19	0.21

Source: Erste Group Research

Income Statement	2006	2007	2008	2009e	2010e	2011e
(IAS, PLN mn, 31/12)	31/12/2006	31/12/2007	31/12/2008	31/12/2009	31/12/2010	31/12/2011
Net sales	**215.48**	**270.94**	**293.52**	**290.28**	**450.40**	**416.56**
Cost of goods sold	-81.64	-122.93	-164.37	-175.77	-177.27	-184.83
Gross profit	**133.84**	**148.01**	**129.15**	**114.52**	**273.14**	**231.72**
SG&A	-85.47	-110.19	-127.86	-152.83	-132.87	-153.09
Other operating revenues	47.16	82.39	15.10	27.58	15.09	12.50
Other operating expenses	-20.67	-12.13	-87.88	-63.86	-31.53	-18.75
EBITDA	**88.54**	**128.81**	**-47.75**	**-45.76**	**153.98**	**104.06**
Depreciation/amortization	-13.68	-20.72	-23.73	-28.84	-30.15	-31.67
EBIT	**74.86**	**108.09**	**-71.49**	**-74.60**	**123.83**	**72.39**
Financial result	32.03	-93.19	-196.52	-13.06	-11.90	-9.12
Extraordinary result	0.00	0.00	0.00	0.00	0.00	0.00
EBT	**106.88**	**14.90**	**-268.00**	**-87.66**	**111.93**	**63.27**
Income taxes	-14.19	11.59	44.97	8.77	-21.27	-12.02
Result from discontinued operations	0.00	0.00	0.00	0.00	0.00	0.00
Minorities and cost of hybrid capital	1.07	1.65	4.14	3.60	3.42	-3.25
Net result after minorities	**93.77**	**28.13**	**-218.89**	**-75.29**	**94.08**	**48.00**

Balance Sheet	2006	2007	2008	2009e	2010e	2011e
(IAS, PLN mn, 31/12)						
Intangible assets	395.91	666.27	1,023.53	1,008.56	1,007.21	1,005.85
Tangible assets	169.23	268.62	488.85	434.90	437.81	441.39
Financial assets	65.01	170.16	181.92	196.26	212.43	230.80
Total fixed assets	**630.14**	**1,105.05**	**1,694.30**	**1,639.73**	**1,657.45**	**1,678.04**
Inventories	61.99	99.63	92.97	93.33	99.19	97.70
Receivables and other current assets	229.77	248.49	215.78	230.13	236.06	233.97
Other assets	0.00	0.00	0.00	0.00	0.00	0.00
Cash and cash equivalents	66.76	47.08	61.72	114.83	184.72	220.50
Total current assets	**358.53**	**395.20**	**370.47**	**438.29**	**519.97**	**552.17**
TOTAL ASSETS	**988.67**	**1,500.26**	**2,064.77**	**2,078.02**	**2,177.42**	**2,230.21**
Shareholders'equity	**787.61**	**871.11**	**1,106.55**	**1,434.01**	**1,444.86**	**1,478.29**
Minorities	**17.53**	**14.44**	**131.14**	**66.03**	**66.03**	**66.03**
Hybrid capital and other reserves	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Pension and other LT personnel accruals	0.00	0.00	0.00	0.00	0.00	0.00
Other LT provisions	0.00	0.00	0.00	0.00	0.00	0.00
Interest-bearing LT debts	7.62	163.87	163.90	81.95	81.13	80.32
Other LT liabilities	60.58	52.22	72.74	76.37	80.19	84.20
Total long-term liabilities	**68.20**	**216.08**	**236.63**	**158.32**	**161.32**	**164.52**
Interest-bearing ST debts	54.33	246.06	328.81	147.97	140.57	133.54
Other ST liabilities	61.00	152.57	261.64	271.70	364.65	387.84
Total short-term liabilities	**115.33**	**398.63**	**590.45**	**419.66**	**505.22**	**521.38**
TOTAL LIAB. , EQUITY	**988.67**	**1,500.25**	**2,064.77**	**2,078.02**	**2,177.42**	**2,230.21**

Cash Flow Statement	2006	2007	2008	2009e	2010e	2011e
(IAS,PLN mn, 31/12)						
Cash flow from operating activities	-7.92	-0.58	37.75	-48.25	106.30	73.96
Cash flow from investing activities	-392.27	-320.52	-289.40	-81.96	-28.20	-30.34
Cash flow from financing activities	454.67	301.42	266.29	183.32	-8.22	-7.84
CHANGE IN CASH , CASH EQU.	**54.48**	**-19.68**	**14.64**	**53.11**	**69.88**	**35.78**

Margins & Ratios	2006	2007	2008	2009e	2010e	2011e
Sales growth	42.1%	25.7%	8.3%	-1.1%	55.2%	-7.5%
EBITDA margin	41.1%	47.5%	-16.3%	-15.8%	34.2%	25.0%
EBIT margin	34.7%	39.9%	-24.4%	-25.7%	27.5%	17.4%
Net profit margin	43.0%	9.8%	-76.0%	-27.2%	20.1%	12.3%
ROE	18.0%	3.4%	-22.1%	-5.9%	6.5%	3.3%
ROCE	15.5%	3.1%	-13.9%	-3.6%	5.9%	3.5%
Equity ratio	81.4%	59.0%	59.9%	72.2%	69.4%	69.2%
Net debt	-4.8	362.8	431.0	115.1	37.0	-6.6
Working capital	243.2	-3.4	-220.0	18.6	14.7	30.8
Capital employed	860.9	1,300.6	1,741.4	1,691.5	1,628.1	1,621.9
Inventory turnover	1.6	1.5	1.7	1.9	1.8	1.9

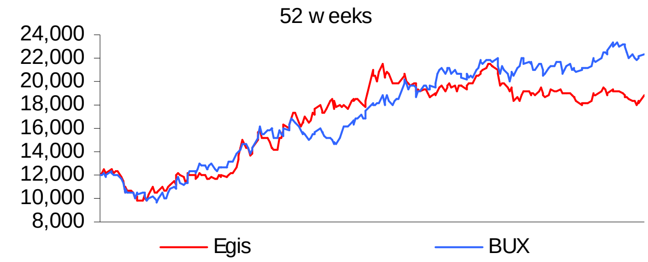
Source: Company data, Erste Group estimates

Company Report – Pharmaceuticals – Hungary – February 3, 2010

Egis Accumulate

Vladimira Urbankova, MBA +43 50100 17343 vladimira.urbankova@erstegroup.com

HUF mn	2008	2009	2010e	2011e
Net sales	96,008.0	107,133.0	107,006.8	114,233.1
EBITDA	16,018.0	20,054.0	21,282.7	24,370.7
EBIT	8,474.0	12,823.0	13,358.5	15,962.0
Net result after min.	13,959.0	12,881.0	13,581.3	15,999.0
EPS (HUF)	1,792.90	1,654.44	1,744.39	2,054.91
CEPS (HUF)	2,740.15	2,656.66	2,758.14	3,130.94
BVPS (HUF)	14,823.78	16,473.08	18,097.47	20,032.38
Div./share (HUF)	120.00	120.00	120.00	120.00
EV/EBITDA (x)	4.6	6.5	5.5	4.6
P/E (x)	6.3	11.8	10.8	9.2
P/CE (x)	4.1	7.4	6.8	6.0
Dividend Yield	1.1%	0.6%	0.6%	0.6%



Performance	12M	6M	3M	1M
in HUF	61.1%	-1.2%	-4.8%	0.2%
in EUR	78.0%	-2.4%	-3.3%	0.3%

Share price (HUF)	18850.00	Reuters	EGIS.BU	Free float	49.1%
Number of shares (mn)	7.8	Bloomberg	EGIS HB	Shareholders	Servier (50.9%)
Market capitalization (HUF mn / EUR mn)	146,761 / 543	Div. Ex-date	18/05/09		
Enterprise value (HUF mn / EUR mn)	118,036 / 437	**Target price**	**21,755.0**	Homepage:	www.egis.hu

High comparative base puts a brake on 2009/10 progress

- **Factoring in only minor adjustments to our Egis model and changing timeframe, our revised DCF-derived 12-month target price arrives at HUF 21,755 per share, slightly below our earlier target of HUF 22,700. Although Egis' lower than average profitability parameters call for a certain discount to its peers, the rally last year closed its valuation gap only partially. After the recent retreat from favor (with some investors taking their profits), valuation multiples are very attractive. While the company's business performance is vulnerable to forint swings, we believe that the risk of a forint-firming dampening effect is more than adequately priced in. All told, we confirm our Accumulate recommendation on the stock.**

- **We have incorporated into our model 1) the changes in accounting policies of the company, slightly lifting its export sales, but (due to cost reshuffling) depressing - in particular - the gross margin; 2) the somewhat bolder progress in Ukraine and other CIS markets, but also less robust outlook for Western European sales in 2010; 3) the revised HUF/USD average exchange rates for 2009 and the coming years. All told, reflecting the acceleration of domestic sales (fueled by new product launches), but the y/y less favorable currency fortunes, we continue to expect Egis' 2009/10 sales to be flat y/y at around HUF 107.0bn). Our 2009/10 net profit target is at HUF 13,581mn, only marginally changed compared to our previous forecast.**

- **Egis' 1Q2009/10 results are expected to demonstrate the beneficial impact of new product launches, counterbalancing the persisting (albeit easing) pricing pressures on its home market. While Russian exports should feel the supportive effect of the ruble appreciation as well as the low comparative base, given the one-off pre-shipments hiking Polish sales in 1Q08/09, we envisage the company's top line retreating by 12.2% y/y to HUF 25,284mn in 1Q09/10. In the absence of the year-earlier one-off boost linked to pre-shipments, as well as the less favorable forex situation, the company's profitability margins are anticipated to head south. We project EBIT slipping 40% y/y to HUF 3,296mn. Despite support from the y/y improving financial result, we expect net profit to fall 30.6% y/y to HUF 3,855mn in 1Q09/10.**

Changes in forecasts / outlook

Ambitious targets for domestic market, new product launches envisaged to lend Egis' sales momentum

While the contribution from new product launches helped to at least partially mitigate the persisting pricing pressures, in the fourth quarter, Egis' sales rose by 1% y/y, sending the 2008/09 domestic sales figure to HUF 29,769mn, up 1.4% y/y. The regulatory measures, particularly the introduction of the international reference pricing system for reimbursed drugs (introduced from January 2010), is becoming a new downside risk for Hungarian pharma manufacturers, including Egis. However, given the lessening price erosion, CFO Laszlo Marosffy has been sticking to the earlier guidance of FY09/10 domestic sales growth of around 5% y/y. Consequently, we leave our 2009/10 domestic sales growth forecast unchanged at 5.0% y/y, translating into the 2009/10 domestic sales target of around HUF 31.3bn. The company's efforts to refresh its product portfolio are gathering pace, with more tangible results to be visible already in 2009/10. However, we do not anticipate that the new products will bring an acceleration of sales, but rather work as an antidote to the stiffening regulations. Consequently, we stick to our projections and envisage Egis' domestic sales advancing by some 5% p.a. in the medium term.

2009/10 export sales to lose forint cushion, 2009/10 tempo foreseen at a negative 2% y/y in HUF terms

Russia/CIS: Egis' sales in Russia plunged 20.6% y/y to USD 25.0mn in 4Q08/09, hampered by the lack of sales of Bioparox (currently under re-registration, due to changes in presentation form). The company continued to focus on the private market; sales within the DLO program were relatively insignificant, at USD 1.1mn in 4Q (and at USD 6.5mn in 2008/09). In total, Egis' sales growth in Russia was tempered to a meager 1.3% y/y, to USD 114.8m. Going forward, CFO Marosffy became more cautious and lowered the guidance for 2009/10 from a 10% rise to 5-10%. After the 3Q recovery, the Ukrainian market saw a q/q contraction (by 28.9% q/q), bringing 2008/09 sales to USD 14.9mn, down 31% y/y. Although Ukraine remains in a laggard position, hampered by the consequences of the sharply depreciating hryvnia and severe toll of the economic crisis on the purchasing power of the population, Egis' CFO envisages sales in Ukraine possibly rising by as much as 20% y/y in USD terms in 2009/10. The low comparative base will provide support here, but this goal still might be difficult to reach with the country still in an economic recession, signs of recovery rather fragile and the regulatory environment shaky. In our opinion, acceleration is in the cards for 2009/10. Consequently, with the Russian market showing the promising recovery recently (with the bolstering effect of the stabilizing ruble, along with rising oil prices), we forecast a 12% y/y rise for Russia/CIS sales (to USD 178.5mn) for 2009/10. At the same time, we slightly increase our target for Russian sales in 2009/10, from a 10% to a 11% y/y rise in USD terms, slightly above the company's guidance.

CEE markets: Weighed down by the negative impact from the regional currencies (namely Polish zloty weakening), coupled with one-off effects (USD 7.5mn revenue related to sales of Anpharma products accounted as a lump sum in 4Q07/08), sales to Eastern Europe dropped by 21.5% y/y to USD 33.6mn in 4Q08/09. (Excluding the one-off element from the comparative base, at a constant currency exchange rate, the growth reached 5% y/y.) In 2008/09, this translated into a 4.7% decline in Egis' Eastern European sales, to USD 133.1mn. Nonetheless, with the above developments already incorporated into our earlier forecasts, and as we continue to believe that the outlook is somewhat brighter (due in part to the regional currencies' stabilization and appreciation in the medium term), we stick to our projections and envisage Egis' sales tempo in the CEE region accelerating to around the 10% to 12% y/y level in the medium term (the next three years). In 2009/10, we see our sales target of USD 157mn as achievable.

Western markets: As indicated by previous interim results, the y/y lower orders from Servier have dragged down API sales in 2008/09. In 4Q alone, bulk chemicals and other sales slid by 27% y/y to USD 10.8mn, sending the full-year total to USD 46.2mn, down 39% y/y. The 2008/09 sales slump of bulk chemicals from their peak in 2007/08 (which was based on stock buildup and high initial deliveries for Servier product launches) was fully in line with expectations and the company's guidance. On the other hand, sales of finished products continued their rally in 4Q08/09 (sales up 70% y/y to USD 7.9mn, fully matching our elevated forecasts). Unfortunately, the outlook for finished pharmaceuticals sales is not as rosy as last year and, reflecting the latest company guidance, we adjust our forecast downwards, envisaging 2009/10 sales in this category retreating 21% y/y, corresponding to sales of around USD 28mn. The order flow from both Servier and other partners for the company's APIs indicates that a further (albeit minor) sales drop is in the cards in 2009/10. We set our 2009/10 target at some USD 42.7mn. (All export figures for 2008/09 as reported.)

Finally, we incorporate into our projections newly revised forex assumptions (annual average exchange rate of HUF 202.3/USD for 2009, from HUF 199.2/USD, and annual average exchange rate of HUF 179.7/USD for 2010, from HUF 178.5/USD). After factoring all of the above-mentioned changes into our sales projections, our 2009/10 sales target is fine-tuned to around HUF 107.0bn, vs. the previous forecast of HUF 107.9bn. For 2010/11, we set our new sales target at HUF 114.2bn. (Here it is worth mentioning that all our new targets are set based on the newly disclosed numbers, with 2008/09 export figures restated by the company. Earlier, according to Hungarian accounting law, shipping costs were deducted from the gross export sales revenue (on average 1% of sales revenue) and the value reduced by shipping costs figured as net sales revenue. From October 1, 2009, according to IFRS, the total sales revenue is shown as sales, while shipping costs are recorded under the general selling costs.)

Change in estimates

Consolidated, IFRS	**2008/9**			**2009/10e**		
(HUF, mn)	**Restated**	**Reported**	*Change*	**Now**	**Before**	*Change*
Net sales	**107,133**	**106,302**	***0.8%***	**107,007**	**107,915**	***-0.8%***
Cost of sales	46,575	42,105	*10.6%*	45,846	43,046	*6.5%*
Gross profit	**60,558**	**64,197**	***-5.7%***	**61,161**	**64,869**	***-5.7%***
Marketing & distr. costs	25,626	24,795	*3.4%*	26,108	25,610	*1.9%*
Administration costs	9,412	13,633	*-31.0%*	9,354	12,942	*-27.7%*
R&D costs	9,957	9,957	*0.0%*	9,945	9,655	*3.0%*
Other oper. exp.	3,944	3,944	*0.0%*	3,612	3,651	*-1.1%*
Other oper. income	1,204	1,204	*0.0%*	1,216	848	*43.4%*
Operating profit	**12,823**	**13,072**	***-1.9%***	**13,359**	**13,858**	***-3.6%***
Financial result	570	570	*0.0%*	1,413	1,335	*5.8%*
Pre-tax profit	**13,393**	**13,642**	***-1.8%***	**14,772**	**15,194**	***-2.8%***
Income taxes	512	512	*0.0%*	1,190	1,245	*-4.4%*
Net income	**12,881**	**13,130**	***-1.9%***	**13,581**	**13,948**	***-2.6%***
Gross margin	56.5%	60.4%		57.2%	60.1%	
EBIT margin	12.0%	12.3%		12.5%	12.8%	
Net margin	12.0%	12.4%		12.7%	12.9%	

Source: Erste Group Research

Favorable changes in sales mix to shore up gross margin

The y/y improving product mix (in particular, the shrinking proportion of bulk chemicals), along with the y/y more favorable forex situation, played in Egis' favor last year, bolstering its profitability parameters. Excluding the effect of accounting changes (for details, please see below) announced recently, Egis' gross margin crossed the 60% mark (reaching 60.4%) in 2008/09. In this respect, the company slightly exceeded our expectations (we had forecast a gross margin of 60.1% in 2008/09). However, the latest changes in the company's accounting policies change the picture. So far, the direct cost of sales had involved direct material costs of production, direct wages and their extras, waste elimination linked expenses as well as costs of the plants. In order to improve decision making and cost management, the company decided (with effect from the 2009/10 fiscal year) to factor into the cost of sales also the costs of quality assurance, logistics costs for raw materials and production management, all of which were earlier accounted for as part of administration costs. In addition, the reversal of the currency fortunes in the coming periods will undoubtedly put a lid on improvements going forward. The restated gross profit in 2008/09 amounted to HUF 60,558mn, corresponding to a gross margin of 56.5%. Consequently, incorporating the accounting change effects into our model, we are forced to reduce our gross margin target to 57.2% for 2009/10. Going forward, despite the ongoing adverse currency trends, we believe that – supported by further improvements in the sales mix - our adjusted gross margin target for FY10/11 of 57.3% is realistic.

Bolstered by currency fortunes, EBIT margin made bold upward move in 2008/09

The 4Q08/09 operating costs were compromised by the rise in sales and marketing expenses (supporting new product launches) and the hike in general and administrative costs (attributed by the company to temporary extra charges related to development of the company, i.e. IT, organizational and personnel changes). With respect to the strong 1-3Q08/09 showing, the operating margin for the full year was lifted to 12.3%, well above the year-earlier 8.8% y/y in 2008/09. Sales and marketing costs rose by 10.2% y/y in 2008/09, lagging behind the sales tempo of 10.7% in the same period, with their share in total sales declining to 23.3%. We opt to remain on the conservative side and, while we factor in the impact from the accounting change (see above), we envisage their share expanding to 24.4% of total sales in 2009/10. With fees for sales representatives reintroduced from mid-February 2009 (hence to be accounted for three quarters of 2008/09 - the same as in the past fiscal year) and domestic sales rising only modestly, payments to the National Health Insurance Fund (OEP) remained practically unchanged y/y at HUF 1.8bn in 2008/09. Nevertheless, here we want to emphasize that, similarly to its home peer Richter, Egis will be able – based on its R&D spending – to skip the obligatory payments to OEP (a 12% rebate on sales of reimbursed drugs and med rep fees) in the future. According to the latest estimates from CFO Marosffy, the positive impact from these legislative changes on Egis' operating profit will be savings of HUF 450mn in the first year and more than HUF 2.0bn in the forthcoming years. The 2008/09 results clearly demonstrated the revamp in the earlier ailing operating profitability. Favorable external conditions were the main factor behind the turnaround.

While the forint appreciation is undoubtedly a negative factor in the coming periods, keeping a lid on the operating line progress, we believe that, helped by tighter cost control, as well as the ongoing favorable changes in the territorial and product mix (falling bulk chemicals sales, expanding share of new products), the company has all prerequisites to stabilize its EBIT margin above the 10% mark. All told, given the slightly less pronounced pace of improvements in 2008/09 (and hence lower comparative base), as well as slightly negative adjustment of the previous year's base (attributable to accounting changes), we fine-tune our operating margin target from 12.8% to 12.5% for 2009/10, setting our new EBIT target at HUF 13,359mn. Our EBIT target for 2010/11 arrives at HUF 15,962mn, corresponding to an EBIT margin of 14.0%. Hampered by the revaluation of investments at loss-making foreign subsidiaries (totaling HUF 1,646mn in 4Q08/09), the financial result slid into negative territory in 4Q; for the full-year 2008/09, the result lagged significantly behind the year-earlier gain (HUF 570mn vs. HUF 6,012mn). Assuming gradually diminishing losses stemming from foreign subsidiaries, as well as less volatile currency fortunes, we leave our 2009/10 financial result forecast broadly unchanged at HUF 1.4bn. All told, our new net profit target arrives at HUF 13,581mn for 2009/10 (vs. the earlier forecast of HUF 13,948mn) and HUF 15,999mn for 2010/11 (down from the previous target of HUF 16,494mn).

1Q09/10 results preview

Egis is scheduled to announce its 1Q09/10 report on February 10, 2010, after market close. We expect net profit of HUF 3,855mn on sales of HUF 25,284mn for October - December 2009, the first quarter of Egis' new fiscal year 2009/10.

Unconsolidated sales preview	1Q 09/10e	1Q 08/09	y/y
Hungary (HUF mn)	7,705	7,317	*5.3%*
Russia (USD mn)	31.9	29.5	*8.0%*
CIS (USD mn)	12.8	9.6	*33.4%*
Eastern Europe (USD mn)	36.7	47.8	*-23.3%*
Other (USD mn)	14.6	21.1	*-31.0%*
Total export (USD mn)	95.9	108.1	*-11.2%*
IFRS unconsolidated	**1Q 09/10e**	**1Q 08/09**	***y/y***
Net sales (HUF mn)	25,284	28,792	*-12.2%*
Operating profit (HUF mn)	3,296	5,490	*-40.0%*
Net income (HUF mn)	3,855	5,555	*-30.6%*
Operating margin	*13.0%*	*19.1%*	
Net margin	*15.2%*	*19.3%*	

Source: Erste Group Research

With the accelerating contribution from new introductions helping to offset the ongoing (albeit lessening) impact of price erosion, we expect Egis' domestic sales to advance by 5.3% y/y (and 2.4% q/q) to HUF 7.7bn in 1Q09/10. The forex situation provides a mixed picture, at least, with the forint slightly weakening vs. the euro, but firming vs. the US dollar y/y in October – December 2009, pointing to diminishing support for exports in HUF terms. Most importantly, in the comparative year-earlier period, the company's results got a substantial boost from pre-shipments to Poland, adding HUF 2,780mn to the top line. Consequently, we think that Egis will be unable to avoid a y/y drop in sales in 1Q09/10. Egis' Eastern European sales are expected to slump 23.3% y/y to USD 36.7mn in 1Q09/10. On the other hand, the comparative base effect plays in favor of y/y improvements in Russia/CIS. The year-earlier period was one of the worst-hit by the onset of the financial crisis in Russia/CIS, with business conditions dramatically deteriorating and forcing the company to cut its deliveries at that time. With Egis' performance in Russia stabilizing, and reflecting the relatively low comparative base, we envisage Egis' Russian sales rising by a solid 8% y/y to USD 31.9mn in 1Q09/10. Although conditions remain a bit more challenging there, Ukraine and other CIS markets are foreseen to make another step forward and Egis' sales tempo is seen at around 33% y/y in 1Q09/10. All this translates into a y/y increase for Egis' Russia/CIS sales in 1Q09/10 of 14.2% y/y to USD 44.7mn. In total, we forecast Egis' sales to Western markets at around USD 14.6mn in 1Q09/10, down 31.0% y/y, out of which finished pharmaceuticals are expected to contribute USD 6.2mn. Weighed down by the ongoing y/y decrease in deliveries of APIs to Servier, sales of bulk chemicals to Western markets are expected to remain sluggish at USD 8.3mn. In summary, we project Egis' sales retreating by 12.2% y/y to HUF 25,284mn in 1Q09/10.

The y/y more favorable sales mix (in particular, the declining proportion of bulk chemicals sales, along with the rising share of new product launches in total sales) should at least partly counterbalance the diminishing currency cushion. Nevertheless, with respect to the absence of the profound bolstering effect from pre-shipments, which buoyed Egis' profitability margins in 1Q08/09, we forecast 1Q09/10 operating profit plunging by 40.0% y/y to HUF 3,296mn, translating into an EBIT margin of 13.0% (down from 19.1% in the year-earlier period). (Excluding the pre-shipment boost, 1Q08/09 EBIT would have reached HUF 3,654mn and the EBIT margin would have stood at 14.0%.) Although the 1Q09/10 financial result is envisaged to end in black territory and somewhat above the year-earlier figure, given the substantial drop on the EBIT line (attributable to the one-off hike in the year-earlier period), we project for 1Q09/10 a rather dramatic 30.6% y/y fall in Egis' net profit to HUF 3,855mn. Excluding the one-off element from the comparative base, the picture is more pleasing, though. We forecast the comparable 1Q09/10 net profit flat y/y.

Valuation Summary

While we decrease our 12-month target price to HUF 21,755 per share, we leave our

Compared to other core CEE countries, the economic situation in Hungary continues to be somewhat more challenging (despite the stabilization), which is reflected in government bond yields remaining considerably above their CEE-based counterparts'. While more rate cuts are still in the cards, we opt to stick to our conservative approach and leave the risk-free rate unchanged at 7.00% for the detailed forecast period of 2010-14. Applying the equity risk premium of 6.75% to the market premium for the forecast period and 6.3% for perpetuity yields WACC of 12.7% for 2010-14 and 11.3% for perpetuity. After incorporating all of the above-mentioned changes to our forecasts into our DCF model (as well as a new timeframe), our DCF-derived 12-month target price amounts to HUF 21,755 per share, slightly below our earlier target price of HUF 22,700.

Accumulate recommendation unchanged

We continue to believe that Egis' share price more than adequately reflects the inherent risks related to the swinging currency fortunes. Furthermore, we think that the currency assumptions and risk associated premiums in our model are very conservative and that the bias is (as before) rather on the upward side. The company's growth tempo will undoubtedly be tempered this year, with the y/y less favorable currency situation taking its toll. Nevertheless, Egis has ample room for improvements, both internally (streamlining of operations and modernization of portfolio) and externally. The company is becoming more active as of lately, speeding up new product registrations and launches, as well as penetrating promising new markets (Turkey). After years of primarily organic growth, Egis aims to expand via acquisitions of smaller generic companies (in CEE, Russia/CIS, Southeast Europe and, eventually, even outside the EU), which are envisaged to offer new growth opportunities, desirable synergy effects and the chance to exploit differences in patent situations. The company has sufficient resources even without tapping financial markets and its balance sheet is in a healthy shape, with practically no external debt and a solid cash pile (of around HUF 20bn at the end of September 2009). Despite the progress in 2008/09, the company's profitability parameters remain below-average and continue to warrant a certain discount to its peers. Nevertheless, even after the stock's rally last year, the valuation gap has closed only partially and multiples are still very attractive. We confirm our Accumulate recommendation.

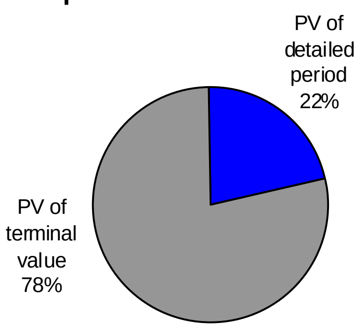
WACC calculation

	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Risk free rate	7.0%	7.0%	7.0%	7.0%	7.0%	5.0%
Equity risk premium	6.8%	6.8%	6.8%	6.8%	6.8%	6.3%
Beta	0.8	0.8	0.8	0.8	0.8	1.0
Cost of equity	**12.7%**	**12.7%**	**12.7%**	**12.7%**	**12.7%**	**11.3%**
Cost of debt	8.5%	8.5%	8.5%	8.5%	8.5%	6.5%
Effective tax rate	10.0%	10.0%	10.0%	10.0%	10.0%	19.0%
After-tax cost of debt	**7.7%**	**7.7%**	**7.7%**	**7.7%**	**7.7%**	**5.3%**
Equity weight	100%	100%	100%	100%	100%	100%
WACC	**12.7%**	**12.7%**	**12.7%**	**12.7%**	**12.7%**	**11.3%**

DCF valuation

(HUF mn)	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Sales growth	*-0.1%*	*6.8%*	*7.4%*	*7.8%*	*7.9%*	*6.0%*
EBIT	13,358.5	15,962.0	17,276.4	18,772.9	20,405.2	21,194.8
EBIT margin	*12.5%*	*14.0%*	*14.1%*	*14.2%*	*14.3%*	*14.0%*
Tax rate	*10.0%*	*10.0%*	*10.0%*	*10.0%*	*10.0%*	*19.0%*
Taxes on EBIT	-1,335.9	-1,596.2	-1,727.6	-1,877.3	-2,040.5	-4,027.0
NOPLAT	**12,022.7**	**14,365.8**	**15,548.8**	**16,895.6**	**18,364.7**	**17,167.8**
+ Depreciation	7,924.2	8,408.6	8,968.9	9,614.8	10,364.8	10,364.8
Capital expenditures / Depreciation	*160.6%*	*160.1%*	*158.6%*	*156.3%*	*153.1%*	*100.0%*
+/- Change in working capital	-846.4	-2,842.7	-3,155.3	-3,353.1	-3,608.0	-2,999.3
Chg. working capital / chg. Sales	*670.5%*	*-39.3%*	*-37.2%*	*-34.9%*	*-34.4%*	*-35.0%*
- Capital expenditures	-12,726.1	-13,461.6	-14,222.9	-15,024.4	-15,868.3	-10,364.8
Free cash flow to the firm	**6,374.4**	**6,470.1**	**7,139.4**	**8,132.8**	**9,253.3**	**14,168.5**
Terminal value growth						*3.0%*
Terminal value						175,826.1
Discounted free cash flow - September 30 2(	5,657.6	5,096.8	4,991.6	5,046.7	5,096.3	94,016.6
Enterprise value - September 30 2009	**119,905.6**					
Minorities	0.0					
Non-operating assets	0.0					
Net debt	-23,139.0					
Other adjustments	0.0					
Equity value - September 30 2009	**143,044.6**					
Number of shares outstanding (mn)	7.8					
Cost of equity	12.7%					
12M target price per share (HUF)	**21,755**					
Current share price (HUF)	18,850					
Up/Downside	*15.4%*					

Enterprise value breakdown



Source: Erste Group Research

Sensitivity (per share)

WACC	Terminal value EBIT margin 13.0%	13.5%	14.0%	14.5%	15.0%
10.3%	22,307	23,011	23,714	24,418	25,121
10.8%	21,355	22,014	22,672	23,330	23,989
11.3%	20,518	21,137	**21,755**	22,374	22,993
11.8%	19,776	20,359	20,943	21,527	22,110
12.3%	19,113	19,666	20,218	20,770	21,322

WACC	Terminal value growth 2.0%	2.5%	3.0%	3.5%	4.0%
10.3%	21,755	22,672	23,714	24,910	26,295
10.8%	20,943	21,755	22,672	23,714	24,910
11.3%	20,218	20,943	**21,755**	22,672	23,714
11.8%	19,567	20,218	20,943	21,755	22,672
12.3%	18,979	19,567	20,218	20,943	21,755

Income Statement	**2006**	**2007**	**2008**	**2009**	**2010e**	**2011e**
(IAS, HUF mn, 30/09)	30/09/2006	30/09/2007	30/09/2008	30/09/2009	30/09/2010	30/09/2011
Net sales	**87,361.52**	**92,489.00**	**96,008.00**	**107,133.00**	**107,006.76**	**114,233.13**
Cost of goods sold	-31,497.58	-41,121.00	-41,512.00	-46,575.00	-45,845.58	-48,770.32
Gross profit	**55,863.94**	**51,368.00**	**54,496.00**	**60,558.00**	**61,161.18**	**65,462.81**
SG&A	-31,899.32	-32,919.00	-34,252.00	-35,038.00	-35,461.62	-38,037.58
Other operating revenues	163.76	623.00	944.00	1,204.00	1,216.04	1,217.26
Other operating expenses	-8,649.00	-11,009.00	-12,714.00	-13,901.00	-13,557.07	-12,680.45
EBITDA	**20,944.37**	**14,265.00**	**16,018.00**	**20,054.00**	**21,282.72**	**24,370.65**
Depreciation/amortization	-5,465.00	-6,202.00	-7,544.00	-7,231.00	-7,924.19	-8,408.61
EBIT	**15,479.37**	**8,063.00**	**8,474.00**	**12,823.00**	**13,358.53**	**15,962.04**
Financial result	2,240.38	-155.00	6,012.00	570.00	1,413.09	1,588.49
Extraordinary result	0.00	0.00	0.00	0.00	0.00	0.00
EBT	**17,719.76**	**7,908.00**	**14,486.00**	**13,393.00**	**14,771.62**	**17,550.53**
Income taxes	-2,194.72	-244.00	-527.00	-512.00	-1,190.31	-1,551.57
Result from discontinued operations	0.00	0.00	0.00	0.00	0.00	0.00
Minorities and cost of hybrid capital	0.00	0.00	0.00	0.00	0.00	0.00
Net result after minorities	**15,525.04**	**7,664.00**	**13,959.00**	**12,881.00**	**13,581.31**	**15,998.97**

Balance Sheet	**2006**	**2007**	**2008**	**2009**	**2010e**	**2011e**
(IAS, HUF mn, 30/09)						
Intangible assets	549.03	600.00	3,785.00	4,220.00	2,335.00	1,835.00
Tangible assets	38,838.68	42,582.00	46,793.00	52,505.00	57,156.35	62,225.65
Financial assets	8,693.55	10,140.00	7,661.00	7,966.00	8,531.20	9,810.88
Total fixed assets	**48,081.26**	**53,322.00**	**58,239.00**	**64,691.00**	**68,022.55**	**73,871.53**
Inventories	28,373.09	28,604.00	32,430.00	35,016.00	35,499.36	37,517.73
Receivables and other current assets	20,588.25	22,443.00	25,213.96	25,325.00	25,674.59	27,271.40
Other assets	0.00	0.00	0.00	0.00	0.00	0.00
Cash and cash equivalents	9,606.68	10,778.00	14,447.04	23,139.00	28,724.33	34,304.48
Total current assets	**58,568.02**	**61,825.00**	**72,091.00**	**83,480.00**	**89,898.27**	**99,093.61**
TOTAL ASSETS	**106,649.28**	**115,147.00**	**130,330.00**	**148,171.00**	**157,920.82**	**172,965.13**
Shareholders'equity	**95,658.87**	**102,388.72**	**115,413.72**	**128,254.72**	**140,901.74**	**155,966.42**
Minorities	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Hybrid capital and other reserves	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Pension and other LT personnel accruals	0.00	0.00	0.00	0.00	0.00	0.00
Other LT provisions	1,307.68	1,692.00	1,523.00	2,095.00	2,063.58	2,032.62
Interest-bearing LT debts	0.00	0.00	0.00	0.00	0.00	0.00
Other LT liabilities	0.00	0.00	0.00	0.00	0.00	0.00
Total long-term liabilities	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Interest-bearing ST debts	0.00	0.00	0.00	0.00	0.00	0.00
Other ST liabilities	9,682.73	11,066.29	13,393.29	17,791.29	14,955.51	14,966.09
Total short-term liabilities	**7,309.23**	**9,226.00**	**10,903.00**	**13,672.00**	**13,702.91**	**14,520.66**
TOTAL LIAB. , EQUITY	**106,649.28**	**115,147.00**	**130,330.00**	**148,141.00**	**157,920.82**	**172,965.13**

Cash Flow Statement	**2006**	**2007**	**2008**	**2009**	**2010e**	**2011e**
(IAS,HUF mn, 30/09)						
Cash flow from operating activities	12,307.77	13,694.00	15,443.00	21,987.00	19,245.97	19,976.36
Cash flow from investing activities	-9,028.13	-10,144.00	-17,765.00	-3,973.00	-12,726.06	-13,461.63
Cash flow from financing activities	-2,868.89	-934.29	-934.00	-936.00	-934.59	-934.59
CHANGE IN CASH , CASH EQU.	**410.75**	**2,615.71**	**-3,256.00**	**17,078.00**	**5,585.33**	**5,580.15**

Margins & Ratios	**2006**	**2007**	**2008**	**2009**	**2010e**	**2011e**
Sales growth	20.3%	5.9%	3.8%	11.6%	-0.1%	6.8%
EBITDA margin	24.0%	15.4%	16.7%	18.7%	19.9%	21.3%
EBIT margin	17.7%	8.7%	8.8%	12.0%	12.5%	14.0%
Net profit margin	17.8%	8.3%	14.5%	12.0%	12.7%	14.0%
ROE	17.6%	7.7%	12.8%	10.6%	10.1%	10.8%
ROCE	18.4%	7.9%	13.3%	10.8%	10.8%	12.1%
Equity ratio	89.7%	88.9%	88.6%	86.6%	89.2%	90.2%
Net debt	-9,606.7	-10,778.0	-14,447.0	-23,139.0	-28,724.3	-34,304.5
Working capital	51,258.8	52,599.0	61,188.0	69,808.0	76,195.4	84,572.9
Capital employed	87,359.9	93,302.7	102,489.7	107,210.7	114,241.0	123,694.6
Inventory turnover	1.2	1.4	1.4	1.4	1.3	1.3

Source: Company data, Erste Group estimates

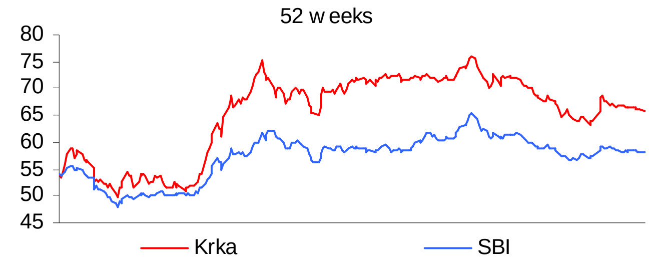
Sector Report – Erste Sector Healthcare

Company Report – Pharmaceuticals – Slovenia – February 3, 2010

Krka Buy

Vladimira Urbankova, MBA +43 50100 17343 vladimira.urbankova@erstegroup.com

EUR mn	2008	2009e	2010e	2011e
Net sales	949.9	951.0	1,017.2	1,110.2
EBITDA	308.4	333.0	318.4	351.9
EBIT	236.8	253.5	230.2	254.8
Net result after min.	156.0	174.8	163.5	184.6
EPS (EUR)	4.40	4.93	4.62	5.21
CEPS (EUR)	6.59	7.11	6.90	7.75
BVPS (EUR)	22.06	26.08	29.65	33.76
Div./share (EUR)	1.05	1.10	1.20	1.40
EV/EBITDA (x)	6.2	7.5	7.8	7.0
P/E (x)	11.0	13.3	14.2	12.6
P/CE (x)	7.3	9.2	9.5	8.5
Dividend Yield	2.2%	1.7%	1.8%	2.1%



Performance	12M	6M	3M	1M
in EUR	21.1%	-7.1%	-9.5%	2.7%

Share price (EUR)	65.76	Reuters	KRKG.LJ	Free float	70.2%
Number of shares (mn)	35.4	Bloomberg	KRKG SV	Shareholders	SOD Fund (15.0%)
Market capitalization (EUR mn)	2,329.6	Div. Ex-date	06/07/09		KAD & PPS (10.2%)
Enterprise value (EUR mn)	2,506.5	**Target price**	**92.0**	Homepage:	www.krka.si

Sleeping beauty

- **Our revised DCF-derived 12-month target price arrives at EUR 92.0 per share. Despite the slowdown last year (partly attributable to unfavorable currency developments, with all regional currencies weakening vs. the euro), Krka's long-term growth prospects remained untouched. Backed by its R&D pipeline (enabling it to follow a patent expiration strategy), complemented by prudent spending policies, it consistently beats its rivals in achieving superior profitability margins. On the other hand, the high profitability parameters do not offer much room for improvement, with the rather scarce news flow keeping a lid on the share price. Nevertheless, in our opinion, the positives prevail and, helped by improved liquidity, the stock is poised to return to its traditional premium to its CEE-based rivals. All told, we stick to our Buy recommendation.**

- **The 2009 preliminary sales report showed that our downward revised full-year sales target of EUR 1,006.2mn for 2009 was still too optimistic, calling for further adjustment in the sales structure, incorporating the slower than envisaged progress in the Russia/CIS region, along with the more subdued tempo in Western European markets. With respect to the solid 1-3Q09 performance (and boost from the reversal of provisions), we project Krka's operating profit rising by 7.0% y/y to EUR 253.5mn in 2009. Factoring in the updated company guidance, we raise our net profit target to EUR 174.8mn for 2009 (vs. the EUR 163.7mn projected earlier).**

- **Going forward, we remain cautiously optimistic. However, reflecting the lower comparative base in certain markets (Russia/CIS, Western Europe), we revise our 2010 forecasts downwards. We project sales of EUR 1,017mn (up 7.0% y/y) in 2010. We continue to believe that, given its strong innovation drive, Krka is well positioned to resist pricing pressures and its profitability should stay at the region's top. We envisage Krka's operating profit at EUR 230.2mn (down 9.2% y/y) and net profit of EUR 163.5mn (down 6.4% y/y) in 2010. Excluding the one-off provisioning effect from the 2009 base, the picture is more pleasing, though. We forecast the comparable EBIT increasing by 9.1% y/y.**

Changes in forecast/outlook

We adjust our 2009 forecasts, incorporating actual sales structure...

...and cut our 2010 sales target to reflect low comparative base

The preliminary 2009 sales figures lagged somewhat behind our original forecasts (while matching the revised company guidance). We are forced to slash our sales projections, while incorporating more adequately the reported preliminary sales performance in individual markets.

CEE markets: As expected, the company sustained a solid tempo (some 6% y/y to EUR 267.6mn, or 28.1% of total sales in 2009) in Central European markets. Going forward, we remain optimistic and believe that the company has all prerequisites to notch a healthy double-digit sales tempo in CEE markets. Anticipating the negative forex impact gradually diminishing and local currency appreciation providing certain relief to regulatory pressures in 2010, we believe that our CEE markets sales target of around EUR 294mn is achievable.

Western Europe: Due to delays, the boost from new product launches was not as robust as originally anticipated. However, the company managed to post a 0.4% y/y sales rise to EUR 225.1mn, or 23.7% of 2009 total sales (from the already high comparative base) in Western Europe and Overseas markets. With new product introductions showing more power, Krka's sales in Western Europe are envisaged to regain momentum. Reflecting the significantly lower than earlier projected 2009 sales, we cut our 2010 sales target in this category to EUR 246.5mn (from EUR 276mn).

Southeast Europe: With Croatian sales hit by pricing pressures (with a new price list coming into effect from March 2009) and Romania hampered by the change to more restrictive drug pricing regulations (as well as a weakening currency impact), SEE market sales remained subdued in 2009 (down by 5% y/y to EUR 128.5mn). We believe that SEE markets should see a recovery from the depressed 2009 levels and continue to project 3.5% sales growth in these territories for 2010. Given the lower starting base, this translates into a new sales target of EUR 133mn, down by 3.7% compared to our previous forecast.

Russia/CIS: Krka's 2009 Russian sales rose by a sound 7% y/y to EUR 168.4mn. Nevertheless, plagued by the troubled Ukrainian market, overall Russia/CIS sales fell by 4% y/y to EUR 224.0mn in 2009 and their share in total Krka sales slipped to 23.6% in 2009, down from the year-earlier 24.4%. Due to the bigger than envisaged slump in CIS sales, the 2010 outlook for Russia/CIS is in absolute terms somewhat less rosy than thought earlier. Nonetheless, the ruble and hryvnia are witnessing stabilization and rising oil prices bode well for an improving situation on the Russian market, including increased purchasing power of consumers. All told, while we anticipate a relatively solid revival in Krka's sales tempo in Russia/CIS this year, we opt to cut our target for Krka's sales in Russia/CIS from EUR 260.8mn to EUR 235.2mn (corresponding to a 5% y/y rise in euro terms) in 2010.

In summary, we lower our sales target for 2009 to EUR 951mn (vs. our original forecast of EUR 1,006.2mn), translating into an 0.1% y/y rise. Krka has all prerequisites to notch a double-digit top line growth pace in the coming years. However, we opt for a cautious approach for 2010, with the shadow of the financial crisis still visible in certain SEE and CIS markets, and fine-tune our projected sales growth rate downward (from 10% to 7%). This, along with the lower comparative base, translates into a reduction of our 2010 consolidated sales target to EUR 1,017.2mn (down from the earlier figure of EUR 1,107.2mn). (This compares with the current company guidance of EUR 1,008mn, corresponding to 6% y/y growth.)

While the 1-3Q09 gross profit reached a still sound 62.7%, it stood slightly below the year-earlier level (of 63.7%), as well as our forecasts. The benefits from the expanding share of new products were wiped out by the negative impact from the regional currencies' weakening and sharp decrease in high-margin Russia/CIS sales. While currency related pressures eased gradually in 4Q09, we opt for a downward adjustment of our forecasts, trimming our gross margin forecast to 62.9% (vs. the earlier projected 63.9%). For 2010, we continue to see regulatory pressures as the biggest threat to Krka's gross profitability and, despite the reversing currency fortunes, we assume only marginal improvements in the gross margin y/y, cutting our target here from 64.0% to 63.0%.

Change in estimates

Consolidated, IFRS (EUR, mn)	2009e Now	2009e Before	2009e Change	2010e Now	2010e Before	2010e Change
Net sales	**951.0**	**1,006.2**	***-5.5%***	**1,017.2**	**1,107.2**	***-8.1%***
Costs of goods sold	353.1	363.3	*-2.8%*	376.1	398.8	*-5.7%*
Gross profit	**597.9**	**642.9**	***-7.0%***	**641.1**	**708.4**	***-9.5%***
Sales & marketing exp.	283.4	251.1	*12.8%*	253.6	277.7	*-8.7%*
R&D expenses	85.1	86.5	*-1.6%*	90.0	94.1	*-4.3%*
General & admin. exp.	73.6	74.9	*-1.8%*	75.3	80.8	*-6.9%*
Other oper. income	97.7	8.1	*1105.6%*	8.0	8.0	*-0.5%*
Operating profit	**253.5**	**238.4**	***6.3%***	**230.2**	**263.8**	***-12.7%***
Financial result	-21.9	-23.0	*-4.7%*	-16.4	-16.6	*-1.3%*
Income taxes	56.7	51.7	*9.7%*	50.3	58.1	*-13.5%*
Minorities	0.1	0.1	*0.0%*	0.1	0.1	*0.0%*
Net income	**174.8**	**163.7**	***6.8%***	**163.5**	**189.0**	***-13.5%***
Gross margin	62.9%	63.9%		63.0%	64.0%	
EBIT margin	26.7%	23.7%		22.6%	23.8%	
Net margin	18.4%	16.3%		16.1%	17.1%	

Source: Erste Group Research

Except for a minor positive difference in R&D expenses, all other 1-3Q09 operating costs were well below our forecasts. The 1-3Q09 sales and marketing costs (falling by 2.9% y/y vs. the reported sales rise of 0.3% y/y) lagged well behind our forecast, prompting us to make another cut to our sales and marketing cost (excluding provisioning impact) estimate, from 25.0% to 24.8% of total 2009 sales. For 2010, we continue to envisage only minor expansion of sales and marketing costs in relative terms, to some 24.9% of total sales. Despite the acceleration in 3Q09, general and administrative costs in 1-3Q09 rose by just 2.6% y/y. We continue to assume these costs stabilizing in the coming periods and stick to our G&A expenditure forecast of around EUR 74mn, corresponding to 7.7% of total 2009 sales. In 2010, reflecting the ongoing cost containment measures, G&A costs are foreseen to lag the top line tempo and their share to decrease to 7.4% of sales. As investments in R&D are to remain a priority, we leave our earlier elevated forecasts for 2009 and 2010 broadly unchanged. With respect to the cut to the top line figure, this translates into an increase in the share of R&D spending in total 2010 sales to around 8.9% (from the earlier estimate of 8.5% of total 2010 sales).

Reversal of provisions far bigger than expected in 2009; unfortunately, same holds for new provision creation

One of the biggest question marks traditionally hangs over the level of necessary new provisioning (weighing on sales and marketing costs) and the release of previous provisions (pushing up other income). Here, the recently released 2009 performance highlights brought a major surprise, forcing us to substantially change our assumptions. Along with its 1Q09 report, Krka disclosed that the European Patent Office (henceforth EPO) has revoked patent EP 848 705, which refers to the active ingredient atorvastatin. The decision of the EPO board of appeal is final, with Warner Lambert, the patentee, having at its disposal only extraordinary remedies, if it believes that its fundamental procedural rights have been violated or a criminal act might have had an impact on the decision. Krka formed provisions for this case of EUR 87.7mn in 2005-08 (as well as a claim for deferred tax assets of EUR 18.4mn). With the litigation finally over, the provisions would be abolished and Krka's net profit would increase by the difference, i.e. EUR 69.3mn. Although the company did not confirm the breakdown of the provisioning related income, reversal of its provisions amounted (according to the recently published preliminary 2009 performance report) to EUR 90mn. Hence, we can assume that the end of the atorvastatin litigation came before the end of 2009. Unfortunately, it was not only the reversal of provisions, but also the scope of the increase of its provisioning for other cases (lowering the benefits from the release of provisions on its 2009 result) that was significantly higher than envisaged. According to the company, the burden from new provisions for potential liabilities associated with the European Commission procedure examining alleged breaches of competition law in the sale of perindopril on EU markets amounted to EUR 47.5mn. All told, we lift our other income forecast from EUR 8.1mn to EUR 97.7mn in 2009. At the same time our adjusted sales and marketing cost forecast arrives at EUR 283.4mn in 2009. Going forward, we assume no major litigation on the horizon and anticipate the level of provisioning decreasing y/y in 2010. We also continue to envisage a somewhat lower level of provisions release. All told, we stick to our earlier forecast of other income of around EUR 8.0mn in 2010. While we prefer to remain on the conservative side, in light of the provisioning push, we see our earlier 2009 operating margin target of 23.7% as too conservative and increase it to 26.7%. Reflecting the downward correction of our top line forecast, but also the buoying effect from the net provisioning balance, we set our new 2009 EBIT target at EUR 253.3mn, above the EUR 238.4mn projected earlier. Excluding the provisioning effect, the EBIT margin is anticipated to reach 22.2% in 2009. For 2010, we project an improvement in the underlying EBIT margin (to 22.6%); our new operating profit target arrives at EUR 230.2mn.

Reflecting new guidance, we increase our 2009 net profit target to EUR 174.8mn

The forex balance was weighed down in 2009 by the weakening of regional currencies vs. the euro. On an encouraging note, after the rather disappointing 1Q09 result, the picture became rosier in the course of the year and, in 3Q09, the financial result ended (contrary to our expectations) in black territory. Consequently, we are prompted to adjust out forecasts accordingly and trim the financial loss forecast for 2009 (from EUR 23.0mn to EUR 21.9mn). In summary, with the help of the improving financial result and (most importantly) the provisioning related hike on the operating level more than counterbalancing the sluggishness of sales, we raise our net profit target for 2009 to EUR 174.8mn, above our earlier target of EUR 163.7mn. For 2010, we assume that, with the regional currencies embarking on an appreciation path vs. the euro (easing not only the pressures on the top line, but also yielding diminishing forex woes), the company has all prerequisites to post solid improvement on the bottom line (excluding the one-off element from the comparative base). Still, with the respect to the lower comparative base, as well as more tempered top line growth, we are forced to revise our 2010 consolidated net profit target downwards to EUR 163.5mn.

4Q09 results preview

As Krka recently released its 2009 sales performance highlights and rough guidance on what to expect on the consolidated bottom line (net profit exceeding EUR 170mn), the full 2009 report (due on February 25, 2010) is not anticipated to bring any surprises, but rather reassure investors that the company, facing numerous challenges, only took a pause in its steep progress last year. While the fourth quarter is traditionally one of the strongest for Krka, the 2009 top line tempo was reported to stay in low single-digit terms. Krka's consolidated sales advanced by a mere 0.1% y/y to EUR 951mn in 2009, out of which the fourth quarter added EUR 261.1mn (down 0.3% y/y). Exports accounted for around 89% of the total consolidated sales in 2009.

Consolidated sales preview

EUR 000	4Q2009e	4Q2008	y/y	1-4Q2009e	1-4Q2008	y/y
Slovenia	26,579	26,808	-0.9%	105,800	104,426	1.3%
South-East Europe	33,382	36,364	-8.2%	128,483	135,388	-5.1%
Russia/CIS	77,772	67,306	15.5%	223,968	232,163	-3.5%
Central Europe	66,265	65,387	1.3%	267,644	253,631	5.5%
Western Europe & Overseas	57,137	66,117	-13.6%	225,114	224,312	0.4%
IFRS consolidated	**4Q2009e**	**4Q2008**	***y/y***	**1-4Q2009e**	**1-4Q2008**	***y/y***
Total sales (EUR 000)	261,135	261,982	*-0.3%*	951,009	949,920	*0.1%*
Operating profit (EUR 000)	98,582	84,962	*16.0%*	253,467	236,781	*7.0%*
Net income (EUR 000)	66,406	45,126	*47.2%*	174,770	155,955	*12.1%*
Operating margin	*37.8%*	*32.4%*		*26.7%*	*24.9%*	
Net margin	*25.4%*	*17.2%*		*18.4%*	*16.4%*	

Source: Erste Group Research

Although we do not expect Krka to repeat or beat its stellar 1Q09 margins (particularly in the current market environment), we believe that q/q improvements in the traditionally strong 4Q are in the cards. We assume that, bolstered by an improving sales mix (apart from an ever-expanding share of new products with higher margins), more favorable territorial sales structure and easing currency linked pressures, Krka will be able to achieve solid q/q progress in gross operating profitability. With respect to the extraordinarily strong 4Q08 showing (with 4Q08 EBIT delivering 35.9% of the 2008 total), a y/y drop in operating profit seemed to be unavoidable. Nevertheless, the latest company information on the reversal of provisions (and creation of new provisions), with a total positive balance of EUR 42.5mn in 2009 on the parent company level, shed new light on the 4Q09 outlook. As before, we assume cost containment measures (particularly in the area of general and administrative expenses) will further bolster the results. All told, helped by the reversal of provisions, we forecast Krka's operating profit to surge by 16% y/y to EUR 98.6mn in 4Q09, sending 2009 EBIT to EUR 253.5mn (up by 7.0% y/y). Assuming a significant y/y improvement in the financial result (with the comparative base weighed down by unfavorable high forex losses), we project net profit amounting to EUR 66.4mn in 4Q09, pushing up the full-year net profit figure to EUR 174.8mn.

Valuation Summary

Krka's home country status results in more advantageous valuation parameters

Krka's home country Slovenia continues to work in favor of the company in terms of its valuation. First, the risk-free rate is lower compared to the one we apply for the home countries of Krka's regional peers. While the current yield of the rather thinly-traded Slovene government bonds is below our earlier forecasts, we opt to remain on the conservative side and leave our risk-free rate assumptions in our DCF model for Krka unchanged at 4.4% for 2010-14. For perpetuity, we continue to apply a risk-free rate of 5%. Secondly, our methodology for setting equity risk premiums is linked to the country's S&P long-term currency rating. Here, Slovenia (with an AA rating) is the top performer in the region. The methodology yields an equity risk premium for the explicitly forecast period at 5.0% and for perpetuity at 4.9%, well below equity risk premiums for Krka's Hungarian peers. Our calculated WACC arrives at 8.2% for 2010-14 and 9.6% for perpetuity. Incorporating the reduced estimates and changing timeframe into our model (compared to our last report from November 2009), we arrive at a new DCF-derived 12-month target price of EUR 92.0 per share, below the earlier value of EUR 103.0 per share.

Currently depressed share price levels are very appealing, although appreciation might take time

Our new target price arrives at EUR 92.0…

…we thus stick to our Buy recommendation

Krka's 2009 interim results clearly demonstrated that the company was not able to completely escape the negative consequences of the economic slowdown on its key markets. Currency related woes took their toll on the only Euro Area-based CEE pharma company in our sector universe. Nevertheless, Krka's profitability margins remained excellent and the company continued to beat all of its peers in this respect. In 2010, Krka's top line tempo is not likely to return to the earlier high double-digit pace, but the outlook is undoubtedly more promising. With regional economies back on a growth path, regional currencies embarking on an appreciation trend and Krka's uninterrupted innovation pace in bringing new generics to the market, the company has all prerequisites to keep its margins at high levels, well exceeding its regional rivals'. Krka's R&D pipeline, full of generic bestsellers waiting for patent expirations, bodes well for the continuation of the company's success story in the coming years and backs up the company's expansion in Western Europe. In addition, Krka's modern generics portfolio continues to fuel the company's sales in its traditional stronghold - CEE countries, including Russia, with the latter market poised to see a revival, supported by the improving economic environment (benefiting from rising oil prices). The stock liquidity, which has taken a hit since the beginning of the financial market crisis, is gradually improving. Moreover, the company is aware of the importance of this issue and is considering measures for improvement, including a possible secondary listing. After Krka's 1-3Q09 results lagged somewhat behind expectations and the company provided rather grim guidance for 2009, the stock came under selling pressure. While there are still some caveats going forward (and with its high profitability, the company set itself a benchmark that is difficult to overcome in the current market conditions), the stock levels are very appealing and inviting for patient investors to gradually build up positions in the undoubtedly best-in-class CEE pharma company. We continue to believe that Krka retains its status as one of the safest (and still attractively valued) fundamental long-term bets in the CEE pharma sector and, should the current risk appetite be somewhat tempered in coming months, with investors rediscovering the beauty of defensive stocks, Krka should be among their first picks. With our DCF-based target price suggesting up to 40% upside potential, we stick to our Buy recommendation on the stock.

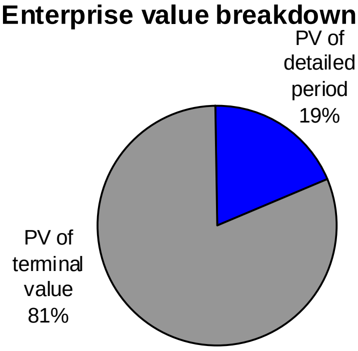
WACC calculation

	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Risk free rate	4.4%	4.4%	4.4%	4.4%	4.4%	5.0%
Equity risk premium	5.0%	5.0%	5.0%	5.0%	5.0%	4.9%
Beta	0.8	0.8	0.8	0.8	0.8	1.0
Cost of equity	**8.6%**	**8.6%**	**8.6%**	**8.6%**	**8.6%**	**9.9%**
Cost of debt	5.9%	5.9%	5.9%	5.9%	5.9%	6.5%
Effective tax rate	23.0%	23.0%	23.0%	23.0%	23.0%	20.0%
After-tax cost of debt	**4.5%**	**4.5%**	**4.5%**	**4.5%**	**4.5%**	**5.2%**
Equity weight	90%	90%	90%	90%	90%	93%
WACC	**8.2%**	**8.2%**	**8.2%**	**8.2%**	**8.2%**	**9.6%**

DCF valuation

(EUR mn)	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Sales growth	*7.0%*	*9.2%*	*10.1%*	*10.6%*	*11.0%*	*8.0%*
EBIT	230.2	254.8	283.7	315.4	351.7	348.8
EBIT margin	*22.6%*	*23.0%*	*23.2%*	*23.3%*	*23.4%*	*21.5%*
Tax rate	*23.0%*	*23.0%*	*23.0%*	*23.0%*	*23.0%*	*20.0%*
Taxes on EBIT	-52.9	-58.6	-65.3	-72.5	-80.9	-69.8
NOPLAT	**177.3**	**196.2**	**218.5**	**242.8**	**270.8**	**279.0**
+ Depreciation	88.2	97.1	106.8	117.4	129.2	129.2
Capital expenditures / Depreciation	*154.4%*	*135.4%*	*122.2%*	*111.0%*	*100.6%*	*100.0%*
+/- Change in working capital	-28.7	-35.7	-43.1	-49.8	-57.0	-48.1
Chg. working capital / chg. Sales	*-43.4%*	*-38.4%*	*-38.4%*	*-38.3%*	*-38.2%*	*-40.0%*
- Capital expenditures	-136.3	-131.4	-130.4	-130.3	-129.9	-129.2
Free cash flow to the firm	**100.6**	**126.1**	**151.7**	**180.1**	**213.2**	**230.9**
Terminal value growth						*3.5%*
Terminal value						3,930.1
Discounted free cash flow - Dec 31 2009	92.9	107.8	119.8	131.5	143.9	2,562.9
Enterprise value - Dec 31 2009	**3,158.9**					
Minorities	1.8					
Non-operating assets	0.0					
Net debt	175.0					
Other adjustments	0.0					
Equity value - Dec 31 2009	**2,982.0**					
Number of shares outstanding (mn)	35.4					
Cost of equity	8.6%					
12M target price per share (EUR)	**92.0**					
Current share price (EUR)	65.8					
Up/Downside	*40.0%*					

Enterprise value breakdown



Source: Erste Group Research

Sensitivity (per share)

WACC	Terminal value EBIT margin 20.5%	21.0%	21.5%	22.0%	22.5%
8.6%	102.3	105.0	107.6	110.3	112.9
9.1%	94.3	96.7	99.1	101.6	104.0
9.6%	87.6	89.8	**92.0**	94.3	96.5
10.1%	81.9	84.0	86.0	88.1	90.1
10.6%	77.1	79.0	80.9	82.8	84.7

WACC	Terminal value growth 2.5%	3.0%	3.5%	4.0%	4.5%
8.6%	92.0	99.1	107.6	117.9	130.8
9.1%	86.0	92.0	99.1	107.6	117.9
9.6%	80.9	86.0	**92.0**	99.1	107.6
10.1%	76.4	80.9	86.0	92.0	99.1
10.6%	72.5	76.4	80.9	86.0	92.0

Income Statement	**2006**	**2007**	**2008**	**2009e**	**2010e**	**2011e**
(IAS, EUR mn, 31/12)	31/12/2006	31/12/2007	31/12/2008	31/12/2009	31/12/2010	31/12/2011
Net sales	**667.95**	**780.92**	**949.92**	**951.01**	**1,017.17**	**1,110.24**
Cost of goods sold	-248.99	-282.83	-325.10	-353.14	-376.10	-409.90
Gross profit	**418.97**	**498.09**	**624.82**	**597.87**	**641.07**	**700.34**
SG&A	-219.39	-259.10	-311.91	-356.94	-328.82	-357.25
Other operating revenues	3.56	3.73	8.62	97.66	7.98	7.77
Other operating expenses	-52.65	-59.07	-84.75	-85.12	-90.02	-96.04
EBITDA	**198.20**	**240.59**	**308.39**	**332.95**	**318.44**	**351.88**
Depreciation/amortization	-47.70	-56.94	-71.61	-79.49	-88.23	-97.05
EBIT	**150.50**	**183.64**	**236.78**	**253.47**	**230.21**	**254.83**
Financial result	-1.74	-8.71	-31.15	-21.89	-16.38	-14.99
Extraordinary result	0.00	0.00	0.00	0.00	0.00	0.00
EBT	**148.76**	**174.93**	**205.63**	**231.58**	**213.83**	**239.84**
Income taxes	-36.67	-42.08	-49.74	-56.74	-50.25	-55.16
Result from discontinued operations	0.00	0.00	0.00	0.00	0.00	0.00
Minorities and cost of hybrid capital	-0.41	-0.30	0.06	-0.07	-0.08	-0.09
Net result after minorities	**111.68**	**132.55**	**155.96**	**174.77**	**163.50**	**184.59**

Balance Sheet	**2006**	**2007**	**2008**	**2009e**	**2010e**	**2011e**
(IAS, EUR mn, 31/12)						
Intangible assets	23.61	129.85	128.98	127.53	126.15	124.85
Tangible assets	506.82	572.24	638.33	714.93	793.58	880.87
Financial assets	44.42	47.61	44.84	56.06	70.07	94.59
Total fixed assets	**574.85**	**749.71**	**812.16**	**898.52**	**989.80**	**1,100.31**
Inventories	115.93	171.65	211.66	212.22	224.72	242.83
Receivables and other current assets	177.96	184.54	239.61	248.74	270.47	295.75
Other assets	0.00	0.00	0.00	0.00	0.00	0.00
Cash and cash equivalents	10.40	15.78	7.60	10.46	13.59	17.67
Total current assets	**304.28**	**371.97**	**458.88**	**471.42**	**508.78**	**556.25**
TOTAL ASSETS	**879.13**	**1,121.68**	**1,271.04**	**1,369.94**	**1,498.58**	**1,656.56**
Shareholders'equity	**563.00**	**670.88**	**781.47**	**924.01**	**1,050.31**	**1,195.92**
Minorities	**7.91**	**10.04**	**1.82**	**1.82**	**1.82**	**1.82**
Hybrid capital and other reserves	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Pension and other LT personnel accruals	0.00	0.00	0.00	0.00	0.00	0.00
Other LT provisions	122.55	143.64	149.66	147.42	140.05	133.04
Interest-bearing LT debts	34.58	87.18	83.73	83.73	75.36	64.06
Other LT liabilities	6.80	21.56	24.13	18.74	11.74	9.98
Total long-term liabilities	**41.39**	**108.74**	**107.86**	**102.47**	**87.10**	**74.03**
Interest-bearing ST debts	55.79	66.14	110.64	101.73	102.37	101.10
Other ST liabilities	88.49	122.25	119.57	92.49	116.93	150.63
Total short-term liabilities	**144.28**	**188.39**	**230.21**	**194.22**	**219.31**	**251.73**
TOTAL LIAB. , EQUITY	**879.13**	**1,121.68**	**1,271.04**	**1,369.94**	**1,498.58**	**1,656.56**

Cash Flow Statement	**2006**	**2007**	**2008**	**2009e**	**2010e**	**2011e**
(IAS,EUR mn, 31/12)						
Cash flow from operating activities	140.63	175.20	150.23	191.05	193.46	197.62
Cash flow from investing activities	-111.54	-204.95	-192.01	-139.84	-136.25	-131.45
Cash flow from financing activities	-30.97	35.14	-6.48	-48.36	-54.07	-62.10
CHANGE IN CASH , CASH EQU.	**-1.87**	**5.39**	**-48.26**	**2.85**	**3.14**	**4.08**

Margins & Ratios	**2006**	**2007**	**2008**	**2009e**	**2010e**	**2011e**
Sales growth	20.5%	16.9%	21.6%	0.1%	7.0%	9.2%
EBITDA margin	29.7%	30.8%	32.5%	35.0%	31.3%	31.7%
EBIT margin	22.5%	23.5%	24.9%	26.7%	22.6%	23.0%
Net profit margin	16.8%	17.0%	16.4%	18.4%	16.1%	16.6%
ROE	21.6%	21.5%	21.5%	20.5%	16.6%	16.4%
ROCE	15.6%	15.4%	15.3%	14.9%	12.7%	13.2%
Equity ratio	64.9%	60.7%	61.6%	67.6%	70.2%	72.3%
Net debt	80.0	137.5	186.8	175.0	164.1	147.5
Working capital	160.0	183.6	228.7	277.2	289.5	304.5
Capital employed	780.2	983.6	1,143.9	1,267.0	1,368.1	1,488.3
Inventory turnover	2.1	2.0	1.7	1.7	1.7	1.8

Source: Company data, Erste Group estimates

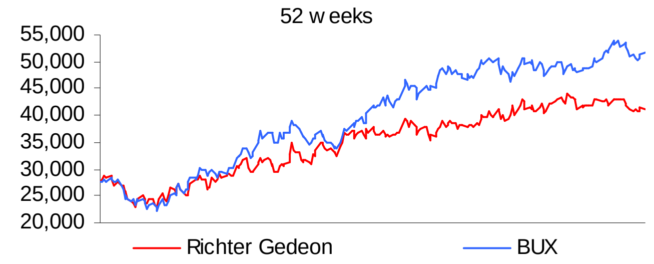
Sector Report – Erste Sector Healthcare

Company Report – Pharmaceuticals – Hungary – February 3, 2010

Richter Gedeon Accumulate

Vladimira Urbankova, MBA +43 50100 17343 vladimira.urbankova@erstegroup.com

HUF mn	2008	2009e	2010e	2011e
Net sales	236,518.0	263,989.0	275,794.1	301,731.5
EBITDA	54,739.0	68,462.0	72,829.8	81,732.7
EBIT	34,156.0	47,179.1	49,517.2	56,286.7
Net result after min.	41,410.0	47,838.9	48,881.5	55,875.2
EPS (HUF)	2,221.87	2,566.81	2,622.75	2,998.00
CEPS (HUF)	3,326.25	3,708.75	3,873.60	4,363.31
BVPS (HUF)	18,054.96	19,875.93	21,848.68	24,146.68
Div./share (HUF)	590.00	600.00	650.00	700.00
EV/EBITDA (x)	8.4	9.8	8.8	7.4
P/E (x)	12.8	16.1	15.7	13.7
P/CE (x)	8.5	11.1	10.6	9.4
Dividend Yield	2.1%	1.5%	1.6%	1.7%



Performance	12M	6M	3M	1M
in HUF	55.2%	11.5%	5.4%	-4.0%
in EUR	71.4%	10.1%	7.0%	-3.9%

Share price (HUF)	41200.00	Reuters	GDRB.BU	Free float	74.6%
Number of shares (mn)	18.6	Bloomberg	RICHT HB	Shareholders	Hungarian State (25.1%)
Market capitalization (HUF mn / EUR mn)	767,864 / 2,843	Div. Ex-date	04/06/09		
Enterprise value (HUF mn / EUR mn)	674,085 / 2,496	**Target price**	**48,200.0**	Homepage:	www.richter.hu

R&D progress to spark share price

- **Richter's investment story is set to gain attractiveness this year. The news flow on its R&D cooperation on CNS drugs with Forest Laboratories should intensify, with progress in the most advanced candidates (RGH-188) assuring that the stock is in the spotlight. Although the forint took an appreciation path, the change is not envisaged to be steep and the company, solidly backed by its excellent territorial (with a strong foothold in the CEE region, including Russia/CIS) and product (gynecological portfolio) niche strategy, should be able to post solid y/y improvements on its top and bottom lines in 2010. Its healthy balance sheet (featuring a heavy cash pile) and stock liquidity (well ahead of its CEE pharma sector peers') provide further arguments to assure the stock its firm place in investment portfolios. Our revised DCF-derived 12-month target price of HUF 48,200 per share suggests that the stock's upside potential has yet to evaporate. Accumulate maintained.**

- **The most important changes to our model include the following: 1) the more favorable than envisaged sales developments in the US; 2) the stronger than anticipated pickup in Russian sales; 3) the sluggish tempo in certain CEE markets (namely Poland, with a negative impact from the zloty weakening); 4) better than envisaged profitability margins (partly due the beneficial impact of US drospirenone linked revenues). Consequently, we raise our consolidated net profit target for 2009 to HUF 47,839mn, on sales of HUF 263,989mn, up 2.1% and 5.3%, respectively. For 2010, we set a new net profit target of HUF 48,882mn, on sales of HUF 275,794mn.**

- **While no exact date for its 4Q09 results release is known yet, the company is expected to publish its report in the second week of February. We project Richter's consolidated sales advancing by 2.7% y/y to HUF 66,915mn in 4Q09. The strong US showing is envisaged to be accompanied by y/y recovering Russian sales. We project a solid upturn in operating profitability (with 4Q09 EBIT up 66.4% y/y). While the forint's q/q stabilization bodes well for keeping the financial result in black numbers, with respect to the year-earlier high comparative base, we envisage net profit to decrease by 24.6% y/y to HUF 10,548mn in 4Q09.**

Changes in forecasts/outlook

Domestic market stabilized, drospirenone contract sent US sales to new highs in 2009

Domestic market: The 2009 interim results provided compelling evidence that the worst is over for Richter in its home market. Despite persistent pricing pressures (related to the quarterly updated changes in reference prices), Richter's domestic sales stabilized and the company managed to post a 4.4% y/y sales rise in 1-3Q09. 3Q09 sales were 3.5% ahead of our forecasts. Consequently, we opt to make just a small upward fine-tuning of our 2009 consolidated domestic sales target from HUF 31.2bn to HUF 31.5bn (corresponding to a 3% y/y rise). For 2010, we remain cautiously optimistic and continue to forecast around 3% y/y growth in Richter's domestic sales, to HUF 32.4bn.

EU: Richter's exports to EU markets were sluggish in the first nine months of 2009. Apart from the mounting competitive pressures in Western Europe, the company had to weather the unfavorable impact of the regional currencies' depreciation (with the Polish zloty weakening, in particular, hurting its sales). Incorporating the less favorable than anticipated performance in the key Polish market, we trim our forecast for Richter's sales to the EU to EUR 362.2mn, corresponding to a 6.9% y/y drop. (This compares with the earlier estimated decrease of around 5.0% y/y to EUR 369.5mn in 2009.) For 2010, we continue to envisage a recovery, with sales there advancing 8.5% y/y to EUR 393.1mn.

Russia/CIS: Reflecting the year-earlier high comparative base (namely in crisis-plagued Ukraine), as well as the much less favorable currency situation, 3Q09 Russia/CIS sales retreated by 7.7% y/y. Nevertheless, they ended 4.1% ahead of our expectations. Also, going forward, the outlook seems to be brighter than originally thought. The more stable currency outlook and rising oil prices (an important factor for improving the Russian economic environment) bode well for the 4Q09 figures and 2010 prospects. Consequently, the company lifted its guidance for Russian sales, which are now expected to be flat or to rise by up to 5% y/y, vs. the earlier expected 0% to 5% y/y drop (in euro terms) in 2009. Also in Ukraine, where the macroeconomic picture is still gloomier than in Russia, Richter's guidance was raised, with 2009 sales now envisaged to fall by 30% to 35% y/y (slightly better than the earlier assumed 30% to 40% y/y slump) in USD terms. We remain slightly more optimistic going forward. For Russia alone, we increase our 2009 sales forecast from around EUR 200mn to EUR 209.6mn, corresponding to an 8% y/y growth (up from the earlier projected 3% y/y rise). While the situation in other CIS markets is still far less satisfactory, with problems reported in Kazakhstan (but some improvements in the cards in Ukraine), we raise our Russia/CIS sales target from EUR 283.3mn to EUR 293.9mn in 2009 (translating into a 0.3% y/y growth in EUR terms vs. the earlier assumed 3.3% y/y fall). For 2010, we stick to our sales growth target for Russia/CIS of 10% y/y, translating into sales of EUR 323.3mn.

US: Although the company remains tightlipped about the exact sales breakdown for its US sales, there is no doubt that the profit sharing arrangement with Barr Laboratories on drospirenone was the main engine behind the excellent 3Q09 US sales figure, which again ended above (this time by 3.1%) our optimistic forecast. Hence, we are prompted to increase our 2009 US sales target to EUR 123.2mn (from EUR 108.6mn), translating into a 38% y/y jump. For 2010, given the relatively high comparative base, we assume the tempo will slow down to around a 6% y/y rise to EUR 130.8mn. Finally, we incorporate into our projections the new exchange rate forecast, fine-tuning the average exchange rate from HUF 199.2/USD to HUF 202.3/USD for 2009, and from an average exchange rate of HUF 280.3/EUR to HUF 280.6/EUR for 2009. For 2010, we revise our forecast from the average exchange rate of HUF 178.5/USD to HUF 179.7/USD, but stick to the average exchange rate of HUF 270/EUR. After factoring in all of the above-mentioned changes, our consolidated sales target for 2009 arrives at HUF 264.0bn, slightly above the previous forecast of HUF 258.6bn, with some HUF 41.6bn to be delivered by wholesale and retail operations and HUF 222.4bn to be contributed by the pharmaceutical business segment. For 2010, our new consolidated sales target is at HUF 275.8bn (up from the earlier HUF 271.7bn), out of which HUF 232.1bn is expected to come from the pharmaceutical segment and HUF 43.7bn from the wholesale and retail arm.

Change in estimates

Consolidated, IFRS (HUF, mn)	2009e Now	2009e Before	2009e *Change*	2010e Now	2010e Before	2010e *Change*
Sales	**263,989**	**258,583**	***2.1%***	**275,794**	**271,657**	***1.5%***
Cost of sales	115,689	114,387	*1.1%*	120,500	119,569	*0.8%*
Gross profit	**148,300**	**144,196**	***2.8%***	**155,294**	**152,087**	***2.1%***
Sales & marketing costs	56,626	55,595	*1.9%*	59,158	58,406	*1.3%*
Admin. & general costs	17,291	17,454	*-0.9%*	17,954	17,929	*0.1%*
R&D costs	23,363	23,014	*1.5%*	24,408	24,042	*1.5%*
Other income / expense	-3,841	-3,841	*0.0%*	-4,257	-4,168	*2.1%*
Operating profit	**47,179**	**44,292**	***6.5%***	**49,517**	**47,542**	***4.2%***
Net financial income	4,458	4,761	*-6.4%*	3,251	3,574	*-9.0%*
Taxation	3,615	3,434	*5.3%*	3,694	3,578	*3.2%*
Minorities	-184	-184	*0.0%*	-193	-193	*0.0%*
Net profit	**47,839**	**45,435**	***5.3%***	**48,882**	**47,345**	***3.2%***
Gross margin	56.2%	55.8%		56.3%	56.0%	
EBIT margin	17.9%	17.1%		18.0%	17.5%	
Net margin	18.1%	17.6%		17.7%	17.4%	

Source: Erste Group Research

Forint weaker y/y, milestone payments to bolster profitability margins in 2009

Bolstered by the y/y more favorable currency situation (with the y/y weakening of the Hungarian forint vs. the EUR and USD), further helped by the positive impact from drospirenone profit sharing revenues, Richter's profitability improved significantly in 1-3Q09. A closer look at the data demonstrates that the progress was even slightly ahead of our rather bullish targets, in particular on the gross profit level. As the gross margin in 3Q09 was more robust than we had forecast (55.8%, vs. our estimate of 53.5%), and the US sales keep their momentum (thanks in part to the drospirenone agreement), while Russia sees a revival, we lift our consolidated gross margin target for 2009 from 55.8% to 56.2%. For 2010, we see a gross margin target improvement to 56.3% as achievable. While 3Q09 sales and marketing expenditures were slightly ahead of our estimates, the difference was not significant. Consequently, reflecting the company's unchanged guidance, we opt to leave our 2009 targets untouched in relative terms and continue to forecast sales and marketing costs at around 21.5% of consolidated sales for full-year 2009. Research and development costs were in line with our projections in 3Q09. Apart from currency developments, the final 2009 figure will also depend on the speed of the progress of the clinical trials in cooperation with Forest Laboratories (still difficult to judge). To be on the conservative side, we stick to our earlier raised forecast for R&D expenses of around 8.9% of consolidated 2009 sales. In summary, our new operating profit target arrives at HUF 47,179mn for 2009 (vs. the earlier HUF 44,292mn), corresponding to a consolidated operating profit margin of 17.9%, up from the earlier projected 17.1%. For 2010, we see an operating margin of 18.0% as realistic.

2009 interim results demonstrated the profound impact of the Hungarian currency fortunes on Richter's financial result. The first quarter net financial income of HUF 9.75bn was followed by the second quarter's net financial loss of HUF 7.5bn. In the third quarter, the company's net financial income returned to black territory, reaching HUF 0.69bn. On the cumulative level, the 1-3Q09 gain was thus pushed up to HUF 2,926mn. The structure of the 1-3Q09 result (an HUF 3,804mn unrealized items loss, vs. HUF 6,730mn in realized income) and only negligible weakening of the HUF at the end of the period in 4Q09 suggest that the 2009 net financial result will stay in positive territory. With respect to the slightly lower 1-3Q09 result, we opt to slightly reduce our original forecast for net financial income from HUF 4.8bn to HUF 4.5bn in 2009. Going forward, the Hungarian currency stabilization points to a minimizing of negative surprises for 2010, although high profits are unlikely to be repeated in coming periods (the same holds for deep losses). In summary, assuming an effective tax rate of 7% (due to the higher statutory tax rates abroad compared to Richter's near-tax haven in Hungary), our new consolidated net profit target arrives at HUF 47,839mn for 2009, corresponding to a 15.5% y/y rise. For 2010, due in part to the less supportive currency fortunes, we forecast Richter's consolidated net profit growth to be tempered to just 2% y/y to HUF 48,882mn.

4Q09 results preview

Richter is expected to announce its 4Q09 results in the second week of February 2010 (no precise date is known yet). We forecast 4Q09 net profit of HUF 10,548mn on sales of HUF 66,915mn (consolidated and according to IFRS standards).

Consolidated sales preview	4Q2009e	4Q2008	y/y	1-4Q2009e	1-4Q2008	y/y
Hungary (HUF bn)	7.614	7.711	*-1.3%*	31.485	30.568	*3.0%*
USA (EUR mn)	37.3	35.4	*5.5%*	123.2	89.3	*38.0%*
EU (EUR mn)	97.6	101.6	*-3.9%*	362.2	389.0	*-6.9%*
Russia, CIS (EUR mn)	71.1	67.9	*4.7%*	293.9	292.9	*0.3%*
Other (EUR mn)	13.7	13.5	*1.4%*	49.2	48.7	*1.0%*
Total export (EUR mn)	219.8	218.4	*0.6%*	828.6	819.9	*1.1%*
IFRS consolidated	**4Q2009e**	**4Q2008**	***y/y***	**1-4Q2009e**	**1-4Q2008**	***y/y***
Total sales (HUF mn)	66,915	65,150	*2.7%*	263,989	236,518	*11.6%*
Operating profit (HUF mn)	10,590	6,366	*66.4%*	47,179	34,156	*38.1%*
Net income (HUF mn)	10,548	13,987	*-24.6%*	47,839	41,410	*15.5%*
Operating margin	*15.8%*	*9.8%*		*17.9%*	*14.4%*	
Net margin	*15.8%*	*21.5%*		*18.1%*	*17.5%*	

Source: Erste Group Research

Russian revival, excellent US sales to drive 4Q09 top and operating lines

While the home market pricing pressures are easing, with respect to the relatively high comparative base, we do not assume that the company will be able to post a y/y rise for 4Q09. Furthermore, with respect to the strong 3Q09 performance, we anticipate Richter's consolidated domestic sales retreating by 4.7% q/q (and slipping by 1.3% y/y) to HUF 7.6bn in 4Q09. After the 4.4% y/y sales rise in 1-3Q09, we expect Richter's domestic sales tempo to slow down to 3.0% y/y for the full year 2009. As indicated by previous interim periods, Richter's 4Q09 exports are anticipated to show a mixed picture in the fourth quarter. Propelled by benefits from the profit-sharing agreement on drospirenone, the US sales performance is envisaged to remain shiny in 4Q09. Due to the relatively high comparative base (with the drospirenone effect already included), we forecast US sales rising by just 5.5% y/y to EUR 37.3mn in 4Q09 (this translates into a stellar 2009 US sales tempo of 38.0% y/y.) Mirroring the stabilization of the situation in the Russian market (helped by the improving currency picture), after a sizable q/q sales decline in 3Q, sales in Russia are expected to regain momentum, advancing by 9.3% q/q (and 9.5% y/y) to EUR 52.0mn in 4Q09. While the recovery of other CIS markets is somewhat less pronounced, the positive effect of the year-earlier low comparative base minimized the scope of the y/y sales deterioration in Ukraine and other CIS markets in 4Q09. All told, we expect Richter's Russia/CIS sales to advance by 4.7% y/y to EUR 71.1mn in 4Q09. On the other hand, the EU area is likely to remain in the doldrums. Despite the ongoing q/q strengthening of some regional currencies (in particular the PLN), we envisage Richter's EU sales sliding by 3.9% in EUR terms (to EUR 97.6mn). In summary, we project Richter's exports increasing by a mere 0.6% y/y in EUR terms in 4Q09. Reflecting the lessening help from the currency side (with the Hungarian forint weakening vs. the EUR, but appreciating vs. the USD), we forecast Richter's consolidated sales advancing by 2.7% y/y to HUF 66.9bn in 4Q09.

However, high comparative base to put lid on y/y progress on bottom line

In 4Q09, the y/y currency developments indicate a still supportive impact (albeit gradually diminishing) on Richter's profitability margins, with the average HUF/EUR exchange rate at 270.9 in 4Q09 (vs. the average of 262.4 in 4Q08). Nonetheless, as 4Q08 represents a relatively low comparative base, the y/y progress should still be sound. However, as before, the y/y more favorable home currency fortunes, coupled with benefits from the drospirenone profit-sharing agreement, were partly wiped out by the deteriorating territorial sales mix and pricing pressures in CEE markets. All told, on the consolidated level, we project operating profit to surge by 66.4% y/y to HUF 10,590mn, translating into an EBIT margin of 15.8% in 4Q09 (this compares with an EBIT margin of 9.8% in 4Q08). Nevertheless, the closing exchange rate as of December 31, 2009, HUF/EUR 270.84, was only slightly changed from the 270.36 seen on September 30, 2009, indicating only a minor improvement q/q for Richter's receivables/payables balance. Still, given the previous year's comparative base (with the best interim financial result of 2008, an HUF 7.6bn financial gain), the y/y worsening is unavoidable. We project the 4Q09 consolidated financial result remaining in positive territory, at an HUF 1bn profit, but still (due to the high year-earlier comparative base) resulting in a deep y/y dive. Hence, despite the bold move on the operating line, we assume that the bottom line to fall by 24.6% y/y, to HUF 10,548mn.

Valuation Summary

We raise our 12-month target price to HUF 48,200 per share and stick to Accumulate

Finally, we have reviewed the parameters of our DCF model. In line with our previous sector report from November 2009, we use the methodology for setting equity risk premiums based on S&P long-term currency ratings. With no major changes in the home country ratings, we stick to the equity risk premium of 6.75% for the explicit forecast period of 2010-14 and to 6.3% for perpetuity. We also opt to leave unchanged our earlier revised risk-free rate assumption (mirroring decreasing yields on Hungarian government bonds in November 2009, we made a cut from 8.5% to 7.0% for the detailed forecast period of 2010-14). Consequently, we stick to a WACC of 12.6% for 2010-14 and 11.3% for perpetuity. All told, reflecting the revised earnings projections as well as changing timeframe, our DCF-derived 12-month target price arrives at HUF 48,200 per share, above our earlier target of HUF 45,900 per share. We continue to believe that there is still some bias on the upward side, with Hungarian government bond yields assumed to stay on a downward trajectory in the course of 2010. Most importantly, Richter's upcoming news flow is set to bring more attention to the company's unique proposition in the region, as the company is the only CEE generics player with a chance to bring (in cooperation with its US partner Forest Laboratories) an original drug to the market. The company promised to inform investors about the result from clinical phase II studies on its original compound RGH-188 for schizophrenia indication. The clinical trials were conducted by Forest Laboratories. Should the outcome be positive, the project is envisaged to move into phase III trials as soon as in 1H10 (along with a parallel study on its use for bipolar mania). The triggering of a milestone payment to Richter is to follow. However, more importantly, along with the progress of the clinical studies, the visibility of the impact of the company's R&D foray will improve. The market will get more data, allowing it to adequately incorporate its impact on Richter's valuation. This would undoubtedly lead to a lift of the target price, as most analysts - including us - have thus far factored in only elevated R&D costs, but no rewards from this R&D project, which could result in the launch of a new drug in 2013/14. We continue to believe that Richter's current share price retains its long-term appeal. Consequently, we stick to our Accumulate recommendation.

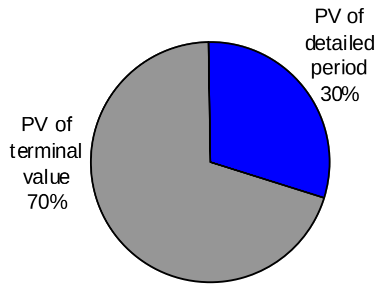
WACC calculation

	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Risk free rate	7.0%	7.0%	7.0%	7.0%	7.0%	5.0%
Equity risk premium	6.8%	6.8%	6.8%	6.8%	6.8%	6.3%
Beta	0.8	0.8	0.8	0.8	0.8	1.0
Cost of equity	**12.7%**	**12.7%**	**12.7%**	**12.7%**	**12.7%**	**11.3%**
Cost of debt	8.5%	8.5%	8.5%	8.5%	8.5%	6.5%
Effective tax rate	7.0%	7.0%	7.0%	7.0%	12.0%	20.0%
After-tax cost of debt	**7.9%**	**7.9%**	**7.9%**	**7.9%**	**7.5%**	**5.2%**
Equity weight	99%	99%	99%	99%	99%	99%
WACC	**12.6%**	**12.6%**	**12.6%**	**12.6%**	**12.6%**	**11.3%**

DCF valuation

(HUF mn)	2010e	2011e	2012e	2013e	2014e	2015e (TV)
Sales growth	*4.5%*	*9.4%*	*9.7%*	*10.6%*	*11.0%*	*8.0%*
EBIT	49,517.2	56,286.7	64,437.5	73,196.0	83,309.1	87,748.5
EBIT margin	*18.0%*	*18.7%*	*19.5%*	*20.0%*	*20.5%*	*20.0%*
Tax rate	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*12.0%*	*20.0%*
Taxes on EBIT	-3,466.2	-3,940.1	-4,510.6	-5,123.7	-9,997.1	-17,549.7
NOPLAT	**46,051.0**	**52,346.7**	**59,926.9**	**68,072.3**	**73,312.0**	**70,198.8**
+ Depreciation	23,312.6	25,445.9	27,879.3	30,712.6	33,745.9	33,745.9
Capital expenditures / Depreciation	*94.1%*	*94.1%*	*94.1%*	*94.2%*	*94.2%*	*100.0%*
+/- Change in working capital	-526.4	-1,079.8	-1,204.8	-1,419.1	-1,599.5	-1,625.0
Chg. working capital / chg. Sales	*-4.5%*	*-4.2%*	*-4.1%*	*-4.1%*	*-4.0%*	*-5.0%*
- Capital expenditures	-21,947.4	-23,950.0	-26,247.8	-28,921.9	-31,778.3	-33,745.9
Free cash flow to the firm	**46,889.8**	**52,762.8**	**60,353.6**	**68,443.9**	**73,680.1**	**68,573.8**
Terminal value growth						*3.5%*
Terminal value						913,575.6
Discounted free cash flow - Dec 31 2009	41,631.2	41,591.9	42,240.1	42,530.2	40,650.6	486,990.8
Enterprise value - Dec 31 2009	**695,634.7**					
Minorities	2,856.7					
Non-operating assets	0.0					
Net debt	-96,636.1					
Other adjustments	0.0					
Equity value - Dec 31 2009	**789,414.2**					
Number of shares outstanding (mn)	18.6					
Cost of equity	12.7%					
12M target price per share (HUF)	**48,200**					
Current share price (HUF)	41,200					
Up/Downside	*17.0%*					

Enterprise value breakdown



Source: Erste Group Research

Sensitivity (per share)

WACC	Terminal value EBIT margin 19.0%	19.5%	20.0%	20.5%	21.0%
10.3%	50,846	51,719	52,592	53,466	54,339
10.8%	48,618	49,432	50,245	51,058	51,872
11.3%	46,678	47,439	**48,200**	48,961	49,722
11.8%	44,972	45,687	46,402	47,117	47,832
12.3%	43,460	44,134	44,809	45,483	46,157

WACC	Terminal value growth 2.5%	3.0%	3.5%	4.0%	4.5%
10.3%	48,200	50,245	52,592	55,314	58,508
10.8%	46,402	48,200	50,245	52,592	55,314
11.3%	44,809	46,402	**48,200**	50,245	52,592
11.8%	43,388	44,809	46,402	48,200	50,245
12.3%	42,112	43,388	44,809	46,402	48,200

Income Statement	2006	2007	2008	2009e	2010e	2011e
(IAS, HUF mn, 31/12)	31/12/2006	31/12/2007	31/12/2008	31/12/2009	31/12/2010	31/12/2011
Net sales	**209,373.00**	**224,076.00**	**236,518.00**	**263,989.01**	**275,794.12**	**301,731.52**
Cost of goods sold	-89,704.00	-104,379.00	-108,421.00	-115,689.24	-120,500.06	-131,239.39
Gross profit	**119,669.00**	**119,697.00**	**128,097.00**	**148,299.78**	**155,294.06**	**170,492.13**
SG&A	-53,050.00	-58,208.00	-67,886.00	-73,916.92	-77,112.03	-83,730.50
Other operating revenues	0.00	0.00	0.00	0.00	0.00	0.00
Other operating expenses	-17,092.00	-25,206.00	-26,055.00	-27,203.79	-28,664.80	-30,474.88
EBITDA	**68,276.00**	**56,496.00**	**54,739.00**	**68,462.00**	**72,829.83**	**81,732.68**
Depreciation/amortization	-18,749.00	-20,213.00	-20,583.00	-21,282.93	-23,312.60	-25,445.93
EBIT	**49,527.00**	**36,283.00**	**34,156.00**	**47,179.07**	**49,517.23**	**56,286.75**
Financial result	2,586.00	-503.00	9,297.00	4,458.11	3,250.94	4,011.86
Extraordinary result	0.00	0.00	0.00	0.00	0.00	0.00
EBT	**52,113.00**	**35,780.00**	**43,453.00**	**51,637.18**	**52,768.16**	**60,298.61**
Income taxes	-711.00	-1,809.00	-1,876.00	-3,614.60	-3,693.77	-4,220.90
Result from discontinued operations	0.00	0.00	0.00	0.00	0.00	0.00
Minorities and cost of hybrid capital	-124.00	-635.00	-167.00	-183.70	-192.89	-202.53
Net result after minorities	**51,278.00**	**33,336.00**	**41,410.00**	**47,838.88**	**48,881.51**	**55,875.18**

Balance Sheet	2006	2007	2008	2009e	2010e	2011e
(IAS, HUF mn, 31/12)						
Intangible assets	6,049.00	11,639.00	15,636.00	13,875.07	16,162.47	17,716.53
Tangible assets	136,049.00	144,863.00	141,935.00	143,486.00	143,286.00	143,586.00
Financial assets	18,579.00	18,985.00	13,486.00	16,857.50	18,121.81	19,888.69
Total fixed assets	**160,677.00**	**175,487.00**	**171,057.00**	**174,218.57**	**177,570.28**	**181,191.22**
Inventories	52,716.00	52,874.00	56,808.00	56,748.47	56,766.50	56,981.50
Receivables and other current assets	53,272.00	64,371.00	79,950.00	83,464.26	85,311.24	89,117.14
Other assets	0.00	0.00	0.00	0.00	0.00	0.00
Cash and cash equivalents	59,119.00	55,231.00	76,318.00	102,004.80	135,159.62	173,340.85
Total current assets	**165,107.00**	**172,476.00**	**213,076.00**	**242,217.54**	**277,237.36**	**319,439.49**
TOTAL ASSETS	**325,784.00**	**347,963.00**	**384,133.00**	**416,436.10**	**454,807.64**	**500,630.71**
Shareholders'equity	**288,115.00**	**306,183.00**	**336,499.00**	**370,437.39**	**407,204.52**	**450,033.46**
Minorities	**5,813.00**	**8,198.00**	**2,787.00**	**2,856.68**	**2,899.53**	**2,943.02**
Hybrid capital and other reserves	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**
Pension and other LT personnel accruals	0.00	0.00	0.00	0.00	0.00	0.00
Other LT provisions	0.00	0.00	0.00	0.00	0.00	0.00
Interest-bearing LT debts	710.00	463.00	70.00	63.00	58.91	54.49
Other LT liabilities	1,775.00	1,249.00	1,029.00	874.65	743.45	631.93
Total long-term liabilities	**2,485.00**	**1,712.00**	**1,099.00**	**937.65**	**802.36**	**686.42**
Interest-bearing ST debts	184.00	392.00	5,053.00	5,305.65	4,775.09	4,297.58
Other ST liabilities	29,187.00	31,478.00	38,695.00	36,898.74	39,126.15	42,670.23
Total short-term liabilities	**29,371.00**	**31,870.00**	**43,748.00**	**42,204.39**	**43,901.23**	**46,967.80**
TOTAL LIAB. , EQUITY	**325,784.00**	**347,963.00**	**384,133.00**	**416,436.10**	**454,807.64**	**500,630.71**

Cash Flow Statement	2006	2007	2008	2009e	2010e	2011e
(IAS,HUF mn, 31/12)						
Cash flow from operating activities	55,501.00	47,736.00	42,417.00	62,508.98	67,751.27	75,659.42
Cash flow from investing activities	-24,150.00	-30,931.00	-35,429.00	-23,556.34	-21,947.42	-23,950.03
Cash flow from financing activities	-12,644.00	-18,137.00	2,131.00	-10,936.84	-12,649.03	-13,528.17
CHANGE IN CASH , CASH EQU.	**18,057.00**	**-1,377.00**	**7,625.00**	**25,686.80**	**33,154.83**	**38,181.22**

Margins & Ratios	2006	2007	2008	2009e	2010e	2011e
Sales growth	21.3%	7.0%	5.6%	11.6%	4.5%	9.4%
EBITDA margin	32.6%	25.2%	23.1%	25.9%	26.4%	27.1%
EBIT margin	23.7%	16.2%	14.4%	17.9%	18.0%	18.7%
Net profit margin	24.6%	15.2%	17.6%	18.2%	17.8%	18.6%
ROE	19.2%	11.2%	12.9%	13.5%	12.6%	13.0%
ROCE	22.3%	12.6%	14.5%	16.5%	16.4%	18.6%
Equity ratio	90.2%	90.3%	88.3%	89.6%	90.2%	90.5%
Net debt	-58,225.0	-54,376.0	-71,195.0	-96,636.1	-130,325.6	-168,988.8
Working capital	135,736.0	140,606.0	169,328.0	200,013.1	233,336.1	272,471.7
Capital employed	237,478.0	261,254.0	269,120.0	277,532.6	280,521.9	284,619.6
Inventory turnover	1.8	2.0	2.0	2.0	2.1	2.3

Source: Company data, Erste Group estimates

Contacts

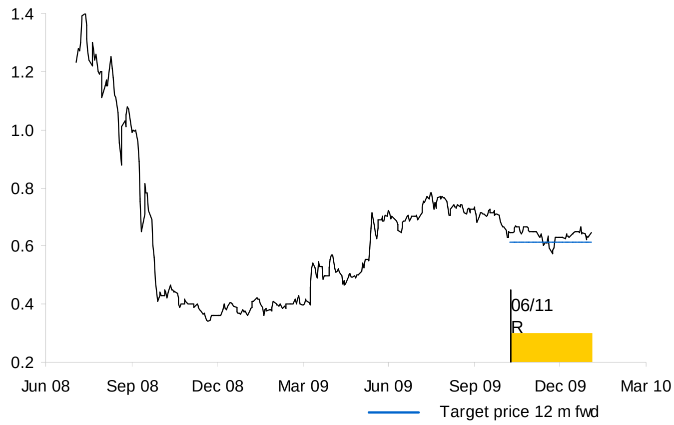
Group Research

Head of Group Research	
Friedrich Mostböck, CEFA	+43 (0)5 0100 - 11902
CEE Equity Research	
Co-Head: Günther Artner, CFA	+43 (0)5 0100 - 11523
Co-Head: Henning Eßkuchen	+43 (0)5 0100 - 19634
Günter Hohberger (Banks)	+43 (0)5 0100 - 17354
Franz Hörl, CFA (Steel, Construction)	+43 (0)5 0100 - 18506
Gernot Jany, CFA (Banks, Real Estate)	+43 (0)5 0100 - 11903
Daniel Lion, CIIA (IT)	+43 (0)5 0100 - 17420
Christoph Schultes, CIIA (Ins., Util.)	+43 (0)5 0100 - 16314
Thomas Unger	+43 (0)5 0100 - 17344
Vera Sutedja, CFA (Telecom)	+43 (0)5 0100 - 11905
Vladimira Urbankova, MBA (Pharma)	+43 (0)5 0100 - 17343
Gerald Walek, CFA (Machinery)	+43 (0)5 0100 - 16360
International Equities	
Hans Engel (Market strategist)	+43 (0)5 0100 - 19835
Stephan Lingnau (Europe)	+43 (0)5 0100 - 16574
Ronald Stöferle (Asia)	+43 (0)5 0100 - 11723
Macro/Fixed Income Research	
Head: Gudrun Egger, CEFA (Euroland)	+43 (0)5 0100 - 11909
Alihan Karadagoglu (Corporates)	+43 (0)5 0100 - 19633
Rainer Singer (US)	+43 (0)5 0100 - 11185
Elena Statelov, CIIA (Corporates)	+43 (0)5 0100 - 19641
Mildred Hager (SW, Japan)	+43 (0)5 0100 - 17331
Macro/Fixed Income Research CEE	
Co-Head CEE: Juraj Kotian (Macro/FI)	+43 (0)5 0100 - 17357
Co-Head CEE: Rainer Singer (Macro/FI)	+43 (0)5 0100 - 11185
Editor Research CEE	
Brett Aarons	+420 233 005 904
Research Croatia/Serbia	
Head: Mladen Dodig	+381 11 22 00 866
Damir Cukman (Equity)	+385 62 37 2812
Alen Kovac (Fixed income)	+385 62 37 1383
Iva Cerovsky (Fixed income)	+385 62 37 1716
Davor Spoljar (Equity)	+385 62 37 2825
Research Czech Republic	
Head: David Navratil (Fixed income)	+420 224 995 439
Petr Bartek (Equity)	+420 224 995 227
Vaclav Kminek (Media)	+420 224 995 289
Jana Krajcova (Fixed income)	+420 224 995 232
Radim Kramule (Oil&Gas)	+420 224 995 213
Martin Lobotka (Fixed income)	+420 224 995 192
Lubos Mokras (Fixed income)	+420 224 995 456
Research Hungary	
Head: József Miró (Equity)	+361 235-5131
Bernadett Papp (Equity)	+361 235-5135
Gergely Gabler (Equity)	+361 253-5133
Orsolya Nyeste (Fixed income)	+361 373-2830
Research Poland	
Head: Artur Iwanski (Equity)	+48 22 330 6253
Magda Zabieglik (Equity)	+48 22 330 6250
Tomasz Kasowicz (Equity)	+48 22 330 6251
Piotr Lopaciuk (Equity)	+48 22 330 6252
Marek Czachor (Equity)	+48 22 330 6254
Wiktor Tymochowicz (Equity)	+48 22 330 6253
Research Romania	
Head: Lucian Claudiu Anghel	+40 21 312 6773
Mihai Caruntu (Equity)	+40 21 311 27 54
Dumitru Dulgheru (Fixed income)	+40 21 312 6773 1028
Cristian Mladin (Fixed income)	+40 21312 6773 1028
Loredana Oancea (Equity)	+40 21311 2754
Eugen Sinca (Fixed income)	+40 21312 6773 1028
Raluca Ungureanu (Equity)	+40 21311 2754
Research Slovakia	
Head: Juraj Barta (Fixed income)	+421 2 4862 4166
Michal Musak (Fixed income)	+421 2 4862 4512
Maria Valachyova (Fixed income)	+421 2 4862 4185
Research Ukraine	
Head: Victor Stefanyshyn (Fixed Income)	+38 044 593 - 1784
Svitlana Bazilevich (Equity)	+38 044 593 - 9286
Maryan Zablotskyy (Fixed income)	+38 044 593 - 9188

Group Institutional & Retail Sales

Institutional Equity Sales Vienna	
Head: Brigitte Zeitlberger-Schmid	+43 (0)5 0100 - 83123
Cash Equity Sales	
Hind Al Jassani	+43 (0)5 0100 - 83111
Werner Fuerst	+43 (0)5 0100 - 83121
Josef Kerekes	+43 (0)5 0100 - 83125
Cormac Lyden	+43 (0)5 0100 - 83127
Neil Owen	+43 (0)5 0100 - 83114
Stefan Raidl	+43 (0)5 0100 - 83113
Simone Rentschler	+43 (0)5 0100 - 83124
Derivative Sales	
Christian Luig	+43 (0)5 0100 - 83181
Manuel Kessler	+43 (0)5 0100 - 83182
Sabine Kircher	+43 (0)5 0100 - 83161
Christian Klikovich	+43 (0)5 0100 - 83162
Armin Pfingstl	+43 (0)5 0100 - 83171
Roman Rafeiner	+43 (0)5 0100 - 83172
Institutional Equity Sales London	
Head: Michal Rizek	+44 20 7623 - 4154
Dieter Benesch	+44 20 7623 - 4154
Tatyana Dachyshyn	+44 20 7623 - 4154
Declan Wooloughan	+44 20 7623 - 4154
Institutional Equity Sales Croatia	
Zeljka Kajkut (Equity)	+38 562 37 28 11
Damir Eror (Equity)	+38 562 37 28 13
Institutional Sales Czech Republic	
Michal Brezna (Equity)	+420 224 995-523
Ondrej Cech (Fixed income)	+420 224 995-577
Michal Rizek	+420 224 995-53
Jiri Smehlik (Equity)	+420 224 995-510
Pavel Zdichynec (Fixed income)	+420 224 995-590
Institutional Sales Hungary	
Gregor Glatzer (Equity)	+361 235-5144
Krisztián Kandik (Equity)	+361 235-5140
Istvan Kovacs (Fixed income)	+361 235-5846
Institutional Equity Sales Poland	
Head: Andrzej Tabor	+4822 330 62 03
Pawel Czuprynski (Equity)	+4822 330 62 12
Lukasz Mitan (Equity)	+4822 330 62 13
Jacek Krysinski (Equity)	+4822 330 62 18
Institutional Equity Sales Slovakia	
Head: Dusan Svitek	+48 62 56 20
Rado Stopiak (Derivatives)	+48 62 56 01
Andrea Slesarova (Client sales)	+48 62 56 27
Saving Banks & Sales Retail	
Head: Thomas Schaufler	+43 (0)5 0100 - 84225
Equity Retail Sales	
Head: Kurt Gerhold	+43 (0)5 0100 - 84232
Fixed Income & Certificate Sales	
Head: Thomas Schaufler	+43 (0)5 0100 - 84225
Treasury Domestic Sales	
Head: Markus Kaller	+43 (0)5 0100 - 84239
Corporate Desk	
Head: Leopold Sokolicek	+43 (0)5 0100 - 84601
Alexandra Blach	+43 (0)5 0100 - 84141
Markus Pistracher	+43 (0)5 0100 - 84100
Roman Friesacher	+43 (0)5 0100 – 84143
Helmut Kirchner	+43 (0)5 0100 – 84144
Christian Skopek	+43 (0)5 0100 - 84146
Fixed Income Institutional Desk	
Head: Thomas Almen	+43 (0)5 0100 - 84323
Martina Fux	+43 (0)5 0100 - 84113
Fixed Income International & High End Sales Vienna	
Jaromir Malak/ Zach Carvell	+43 (0)5 100 - 84254
U. Inhofner/ P. Zagan/ C. Mitu	+43 (0)5 100 - 84254
Fixed Income International Sales London	
Paul Osment/ Simone Pilz	+44 20 7623 4159

Antibiotice

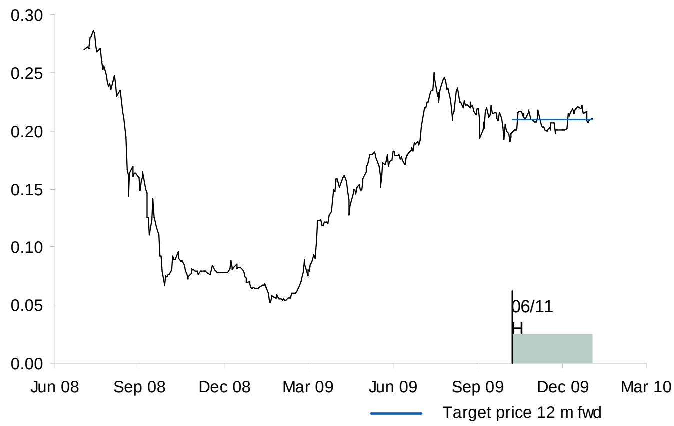


Rating history

Date	Rating	Price	Target Price
06. Nov 09	Reduce	0.65	0.62

Company	Disclosure
Antibiotice	

Biofarm

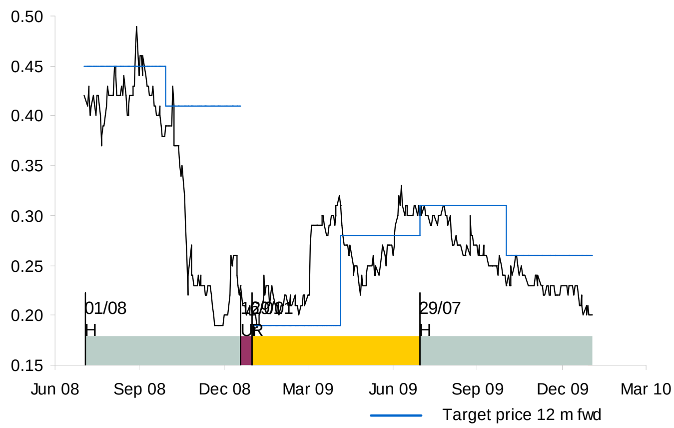


Rating history

Date	Rating	Price	Target Price
06. Nov 09	Hold	0.20	0.21

Company	Disclosure
Biofarm	

Bioton

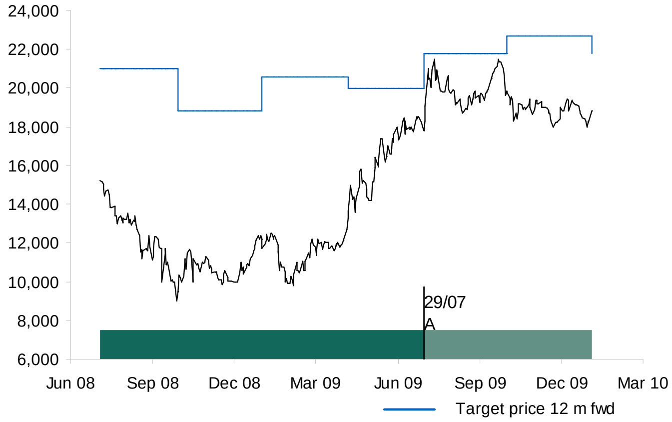


Rating history

Date	Rating	Price	Target Price
29. Jul 09	Hold	0.30	0.31
29. Jan 09	Reduce	0.20	0.19
16. Jan 09	Under review	0.23	
14. Jan 08	Hold	0.94	1.03
15. Jun 07	Accumulate	1.96	2.25

Company	Disclosure
Bioton	

Egis

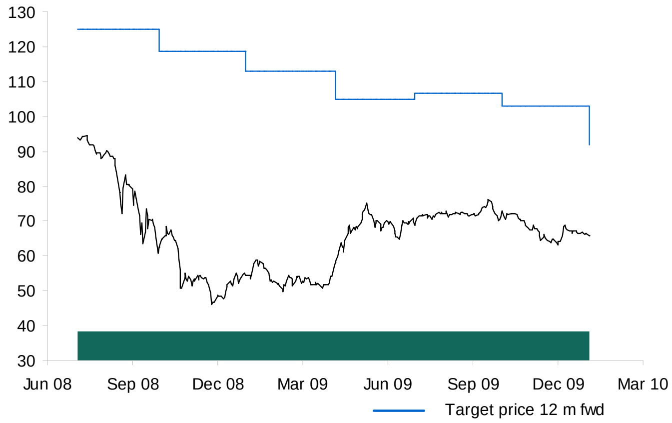


Rating history

Date	Rating	Price	Target Price
29. Jul 09	Accumulate	17800.00	21785.00
27. Feb 08	Buy	18850.00	24400.00
24. Oct 06	Accumulate	26570.00	31120.00
26. May 06	Buy	28820.00	35600.00
17. Aug 05	Accumulate	17995.00	20400.00
20. May 05	Buy	16950.00	20450.00
18. Aug 03	Accumulate	7600.00	11250.00

Company	Disclosure
Egis	

Krka

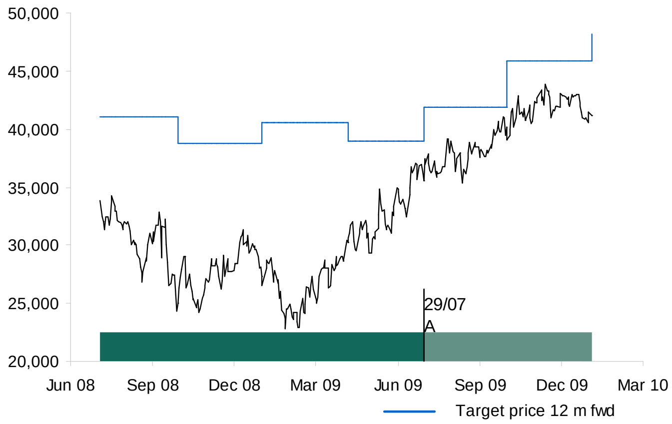


Rating history

Date	Rating	Price	Target Price
30. Nov 07	Buy	113.58	139.50
02. Apr 07	Accumulate	83.05	96.00

Company	Disclosure
Krka	

Richter Gedeon



Rating history

Date	Rating	Price	Target Price
29. Jul 09	Accumulate	35550.00	41900.00
10. Aug 07	Buy	36250.00	46000.00
15. Feb 07	Accumulate	40700.00	46310.00
24. Oct 06	Hold	44000.00	45225.00
19. May 06	Accumulate	42700.00	49350.00
13. Jun 05	Hold	28920.00	29200.00
11. Nov 04	Buy	22400.00	26650.00
10. Nov 04	Accumulate	22400.00	29067.00
11. May 04	Buy	20115.00	26650.00
06. Aug 03	Accumulate	18100.00	19438.00

Company	Disclosure
Richter Gedeon	

Important Disclosures

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Erste Group rating definitions

Buy	> +20% to target price
Accumulate	+10% < target price < +20%
Hold	0% < target price < +10%
Reduce	-10% < target price < 0%
Sell	< -10% to target price

Our target prices are established by determining the fair value of stocks, taking into account additional fundamental factors and news of relevance for the stock price (such as M&A activities, major forthcoming share deals, positive/negative share/sector sentiment, news) and refer to 12 months from now. All recommendations are to be understood relative to our current fundamental valuation of the stock. The recommendation does not indicate any relative performance of the stock vs. a regional or sector benchmark.

Distribution of ratings

	Coverage universe		Inv. banking-relationship	
Recommendation	**No.**	**in %**	**No.**	**in %**
Buy	24	17.9	7	58.3
Accumulate	31	23.1	1	8.3
Hold	37	27.6	2	16.7
Reduce	18	13.4	2	16.7
Sell	10	7.5	0	0.0
N.R./UND.REV./RESTR.	14	10.4	0	0.0
Total	**134**	**100.0**	**12**	**100.0**

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Phone +43 (0)5 0100 - ext.

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