

Report on Valuation of Regulated and Semi-Regulated Business of SMS Pharmaceuticals Limited for the purpose of Demerger

Raju & Prasad

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To

The Board of Directors

SMS Pharmaceuticals Limited

Hyderabad.

Dear Sirs,

Sub: Valuation of Regulated and Semi-Regulated Businesses of SMS Pharmaceuticals Limited as on 31.03.2016.

We refer to the appointment letter dated 1st April, 2016 wherein we have been appointed as the valuers, in connection with the proposed demerger of the Semi-Regulated Business of SMS Pharmaceuticals Limited into SMS Lifesciences India Limited, with effect from 1st April, 2016.

Based on the discussions with the management and on the analysis carried out on the information and explanations received from the management of the company, and after considering the decisions of the Audit Committee in this regard, the value of the Regulated Business is arrived at **Rs. 226,17,79,689/-** and the value of Semi-Regulated Business is arrived at **Rs. 68,18,35,142/-** as at 31.03.2016.

Please feel free to contact us for any further clarification/information on the valuation.

We thank the management and employees of the company for the cooperation extended for the valuation assignment.

Thanking You,
Yours sincerely,

For Raju & Prasad
Chartered Accountants

Y. Bala Krishna Reddy

Y. Bala Krishna Reddy

Partner

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1. Introduction

SMS Pharmaceuticals Limited (hereinafter referred to as "SMS Pharma") (Demerged Company) is engaged in the business of manufacturing of pharmaceutical products. The management of the SMS pharma has proposed to demerge the Semi-Regulated Business (Demerged Undertaking) into a separate company viz., SMS Lifesciences India Limited (hereinafter Referred to as "SMS Lifesciences") (Resulting Company). In connection with the proposed demerger, the Board of Directors of SMS pharma had appointed us, M/s Raju & Prasad Chartered Accountants for arriving at the value of Regulated and Semi-Regulated Business vide appointment letter dated 1st April, 2016.

2. Definitions

2.1 "Demerged Company" means SMS Pharmaceuticals Limited, a company incorporated under the provisions of the Companies Act, 1956 under CIN: **L24239AP1987PLC008066** and having registered office at Plot No.19-III, Road No.71, Opp. Bharatiya Vidya Bhavan School, Jubilee Hills, Hyderabad 500096.

2.2 "Demerged Undertaking" means and include

1. all the business, undertaking, properties, investments and liabilities of whatsoever nature and kind and wheresoever situated, of the Demerged Company, in relation to and pertaining to the Semi-Regulatory Units No. I, IV and V on going concern basis, together with all its assets and liabilities and shall mean and include (without limitation):
 - (a) all the movable and immovable properties including plant and machinery, equipment, furniture, fixtures, vehicles, stocks and inventory, leasehold assets and other contingent assets (whether tangible or intangible) of whatsoever nature in relation to the Semi-Regulatory Units, approvals, consents, letters of intent, registrations, contracts, engagements, arrangements, settlements, rights, credits, titles, interests, benefits, advantages, leasehold rights, sub-letting tenancy rights, with or without the consent of the lessor/landlord as may be required by law, goodwill, other intangibles, industrial and other licenses, permits, authorisations, import quotas and other quota rights, right to use and avail of telephones, telex, facsimile and other communication facilities, connections, installations and equipment, utilities, electricity and electronic and all other services of every kind, nature and description whatsoever, provisions, funds and benefits of all agreements, arrangements, deposits, advances, recoverable and receivables, whether from government, semi-government, local authorities or any other person including customers, contractors or other counter parties, etc., all earnest monies and/or deposits, privileges, liberties, easements, advantages, benefits, exemptions, licenses, privileges concerning the Semi-Regulatory Units and approvals of whatsoever nature (including but not limited to benefits of all tax holiday, tax relief including under the Income Tax Act, 1961 such as credit for advance tax, taxes



deducted at source, brought forward accumulated tax losses, unabsorbed depreciation, etc.) and wheresoever situated, belonging to or in the ownership, power or possession or control of or vested in or granted in favour of or enjoyed by the Demerged Company in relation to the Semi-Regulatory Units as on the Appointed Date;

- (b) all the debts, borrowings, obligations and liabilities, whether present, or future, whether secured or unsecured, of the Demerged Company in relation to the Semi-Regulatory Units as on the Appointed Date comprising of:
- (i) all the debts, duties, obligations and liabilities including contingent liabilities which arise out of the activities or operations of the Demerged company in relation to the Semi-Regulatory Units and all other debts, liabilities, duties, and obligations of the Demerged Company relating to the Demerged Undertaking which may accrue or arise after the Appointed Date but which related to the period up to the day of immediately preceding the Appointed Date;
 - (ii) the specific loans and borrowings raised, incurred and utilised solely for the activities and operations of Demerged Company in relation to the Semi-Regulatory Units; and
 - (iii) liabilities other than those referred to in sub-clauses (i) and (ii) above and not directly relatable to the Semi-Regulatory Units, being the amounts of any general or multipurpose borrowings of Demerged Company as stand in the same proportion which the value of assets transferred under this Clause of Semi-Regulatory Units bears to the total value of the assets of the Demerged Company immediately before the Appointed Date;
- (c) all intellectual property rights, including trademarks, trade names and the goodwill associated therewith, patents, patent rights, copyrights and other industrial designs and intellectual properties and rights of any nature whatsoever including know-how, or any applications for the above, assignments and grants in respect thereof of the Demerged Company in relation to the Semi-Regulatory Units as on the Appointed Date;
- (d) all books, records, files, papers, engineering and process information, records of standard operating procedures, computer programmes along with their licenses, drawings, manuals, date catalogues, quotations, sales and advertising materials, lists of present and former customers and suppliers, customer credit information, customer pricing information and other records whether in physical or electronic form, in connection with or relating to the Semi-Regulatory Units of the Demerged Company as on the Appointed Date;
- (e) all employees of the Demerged Company engaged in the Semi-Regulatory Units; and



(f) any question that may arise as to whether a specific asset (tangible or intangible) or any liability pertains or does not pertain to the Semi-Regulatory Units or whether it arises out of the activities or operations of the Semi-Regulatory Units or not, shall be decided by the Board of the Demerged Company or any committee thereof.

2. Premises located at C-23 Industrial Estate, Sanathnagar Hyderabad,
3. Premises located at D-63, Phase I, IDA Jeedimetla, Hyderabad,
4. Premises located at Flat no. 417, Nilgiri, Aditya Enclave, Ameerpet Hyderabad,
5. Vacant land admeasuring Ac. 19 in plot bearing no. 46 located at Pharma City, Parawada Mandal, Visakhapatnam District, Andhra Pradesh,
6. Investments related to Semi-Regulatory Units.

2.3 **"Regulatory Units"** means, those units which are certified by the authorities of highly regulated markets of United States of America, Europe & Australia and have high entry barriers in terms of intellectual property rights and regulatory requirements, including facility approvals.

2.4 **"Remaining Undertaking"** means all the undertakings, businesses, activities and operations of the Demerged Company other than those comprised in the Demerged Undertaking.

2.5 **"Resulting Company"** means SMS Lifesciences India Limited, a company Incorporated under the provisions of the Companies Act, 1956 under CIN: U74930TG2006PLC050223 and having registered office at Plot No. 265Q, Road No. 10, Jubilee Hills, Hyderabad.

2.6 **"Semi-Regulatory Units"** means, units which are certified on accreditation basis and include rest of the world [apart from markets mentioned under Regulatory Units / except USA, Europe and Australia], which offer low entry barriers in terms of regulatory requirements and intellectual property rights



3. Background

3.1 Background of the Demerged Company i.e. SMS Pharma:

- 3.1.1 SMS Pharmaceuticals Limited (SMS Pharma) is a public limited company incorporated in India in the year 1987. The Company has paid up share capital of Rs.8,46,52,030/- divided into 8,46,52,030 equity shares of Rs.1/- each. The equity shares of SMS Pharma are listed on the Bombay Stock Exchange (BSE) and National Stock Exchange (NSE) with public shareholding of 36.12%. SMS Pharma is primarily engaged in the manufacture and sale of pharmaceutical products broadly classified as Active Pharmaceutical Ingredients (API), Intermediates and other products.
- 3.1.2 The registered office of SMS Pharma is located at Road No.71, Jubilee Hills, Hyderabad and has five manufacturing units and one research and development centre. These units can be categorised into Regulated and Semi-Regulated Businesses.
- 3.1.3 Regulatory Units include,
- Unit-2 – Bachupally, Telangana
 - Unit-7 – Vijayanagaram, Andhra Pradesh
 - R&D Centre – Gagillapur, Telangana
- 3.1.4 Semi-Regulatory Units include,
- Unit-1 – Kazipally, Hyderabad
 - Unit-4 – Jeedimetla, Hyderabad
 - Unit-5 – Bollaram, Hyderabad
 - Other Assets
- 3.1.5 Unit 3 of SMS Pharma is closed since December, 2011 and Unit 6 was sold in the financial year 2012-13.

3.2 Background of Resulting Company i.e. SMS Lifesciences:

- 3.2.1 SMS Lifesciences India Limited was incorporated in the year 2006. Originally, SMS Lifesciences was incorporated as Potluri Real Estate Private Limited in 2006. Later in the year 2014, name of the company was changed to Potluri Packaging Industries Private Limited. Further, in the year 2014, the name has been changed to SMS Lifesciences India Private Limited from Potluri Packaging Industries Private Limited. Later, the company was converted into Public Limited Company with effect from 22.06.2016.
- 3.2.2 Paid up capital of SMS Lifesciences is 10,000 equity shares with face value of Rs. 10/- as on 31st March 2016.
- 3.2.3 The company is engaged in the business of manufacturing, buying, selling, offering consultancy, importing and exporting, acting as commission agents and



generally dealing with all types of organic and inorganic chemicals, pharmaceuticals, drugs and intermediaries.

3.2.4 SMS Lifesciences India Limited has become the wholly owned subsidiary of SMS Pharmaceuticals Limited with effect from 01.04.2016.

3.3 Proposed Demerger:

3.3.1 We understand that the management of SMS Pharma intends to demerge the Semi-Regulated Business into a separate company viz., SMS Lifesciences India Limited, with effect from 1st April, 2016 (Appointed Date). According to the explanations provided to us, the management is proposing demerger to reduce the impact of Semi-Regulated Business on the Regulated Business, achieving operational efficiencies, site synergies and streamlining its current structure. The circumstances, reasons and/or grounds that have necessitated and/or justified the Scheme and advantages thereof are, inter alia, as follows:

- a) The transfer and vesting of the demerged undertaking to the resulting company through this scheme is with a view to unlock the economic value of the demerged undertaking.
- b) The nature of the risk and return involved in the Semi-Regulated Business is distinct from the regulatory units of the demerged company. Hence, transfer of Semi-Regulated Business would enable these units run independently and to evaluate potential independent collaborators and expansion without impacting the demerged company entirely.
- c) Transfer would provide greater flexibility and visibility on the operational and financial performance of the Semi-Regulated Business and would provide higher degree of independence as well as accountability.
- d) The Board of Directors of the demerged company is of the opinion that the demerger would benefit the shareholders, creditors, employees and other stakeholders of both the companies.

3.3.2 The demerger is proposed to be carried out through a scheme of arrangement (Scheme of Demerger) under Section 391 to 394 read with Section 100 to 103 of Companies Act, 1956 and the provisions of Companies Act, 2013, as applicable. Further, it has been explained that the demerger shall be undertaken duly complying with the provisions of Sec 2(19AA) of the Income Tax Act, 1961.

4. Purpose of the valuation assignment

Scope of the present valuation assignment is to arrive at the value of both Regulated Business (Remaining Undertaking) and Semi-Regulated Business (Demerged Undertaking), as per the generally accepted valuation methodologies.

Effective date for the purpose of valuation is 31st March, 2016 (Closing hours)



5. Valuation Methodologies

There are various methodologies that can be used for the valuation of a business undertaking. The methodologies used for valuation depend on the purpose for which the valuation is done. The following are the generally accepted valuation approaches and methods.

5.1 Net Asset Value (NAV) Method

- a) Book value basis (or)
- b) Replacement Cost basis (or)
- c) Realizable Value (Liquidation) basis

5.2 Income Approach

- a) Discounted Cash Flow Method (DCFM)

5.3 Market Approach

- a) Quoted Market Price
- b) Comparable Listed Multiples
- c) Comparable Transaction Multiples

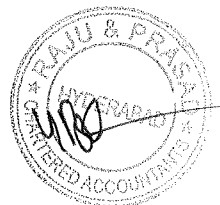
6. Selection of Valuation Methodology

6.1 As per the explanations given to us by the management, the demerger shall be carried out duly complying with the provisions of Sec 2(19AA) of Income Tax Act, 1961.

6.2 As per Section 2 (19AA),

"Demerger", in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 203 of the Companies Act, 2013, by a demerged company of its one or more undertakings to any resulting company in such a manner that—

- i. *all the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger*
- ii. *all the liabilities relatable to the undertaking, being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger*
- iii. *the property and the liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger*



- iv. *the resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis [except where the resulting company itself is a shareholder of the demerged company]*
- v. *the shareholders holding not less than three-fourths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become share-holders of the resulting company or companies by virtue of the demerger otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company*
- vi. *the transfer of the undertaking is on a going concern basis*
- vii. *the demerger is in accordance with the conditions, if any, notified under sub-section (5) of section 72A by the Central Government in this behalf.*

Explanation 1. —For the purposes of this clause, "undertaking" shall include any part of an undertaking, or a unit or division of an undertaking or a business activity taken as a whole, but does not include individual assets or liabilities or any combination thereof not constituting a business activity

Explanation 2. —For the purposes of this clause, the liabilities referred to in sub-clause (ii), shall include—

- a) *the liabilities which arise out of the activities or operations of the undertaking*
- b) *the specific loans or borrowings (including debentures) raised, incurred and utilised solely for the activities or operations of the undertaking; and*
- c) *in cases, other than those referred to in clause (a) or clause (b), so much of the amounts of general or multipurpose borrowings, if any, of the demerged company as stand in the same proportion which the value of the assets transferred in a demerger bears to the total value of the assets of such demerged company immediately before the demerger.*

Explanation 3. —For determining the value of the property referred to in sub-clause (iii), any change in the value of assets consequent to their revaluation shall be ignored.

Explanation 4. —For the purposes of this clause, the splitting up or the reconstruction of any authority or a body constituted or established under a Central, State or Provincial Act, or a local authority or a public sector company, into separate authorities or bodies or local authorities or companies, as the case may be, shall be deemed to be a demerger if such split up or reconstruction fulfils.

6.3 To ensure that the demerger is carried out in a tax neutral manner, all the assets and liabilities of the demerged undertaking shall be transferred at the book value appearing in the books of the demerged company immediately before demerger as required in sub clause (iii) of Section 2(19AA). Hence, the Net Asset Value approach using book values is considered appropriate and accordingly adopted for arriving at the value of the Regulated Business i.e., Remaining Undertaking and Semi-Regulated Business i.e. demerged undertaking



7. Procedures

In this connection, we would like to state that we had relied on the information and explanations given to us and we have conducted a limited review of the audited financials as on 31st March, 2016. The procedures used in our analysis included such substantive steps as we considered necessary under the circumstances, including, but not necessarily limited to the following:

- 7.1 Considered the audited financial statements of SMS Pharma for the year ended 31st March 2016
- 7.2 Considered and relied on segment wise balance sheets as on 31st March, 2016 as given by the management
- 7.3 Interviews, correspondence with the management, explanations and representations given by the management, on which we have relied.
- 7.4 Decisions/recommendations of Audit Committee communicated vide letter dated 08-08-2016.
- 7.5 Such other analysis, reviews and inquiries, as we considered necessary.



8. Value of the Regulated and Semi-Regulated Undertakings

8.1 The following statement of assets and liabilities of both undertakings as provided to us by the management and we relied upon the same for the purpose of valuation:

S.No	Particulars	SMS Pharma (Pre-Demerger)	Regulated (Post-Demerger)	Semi-Regulated (Post-demerger)
I	EQUITY AND LIABILITIES			
1	Shareholders' Funds			
	(a) Share Capital	8,46,52,030	8,46,52,030	-
	(b) Reserves & Surplus	285,89,62,801	217,71,27,659	68,18,35,142
		294,36,14,831	226,17,79,689	68,18,35,142
2	Non-Current Liabilities			
	(a) Long Term Borrowings	113,22,49,944	89,73,36,834	23,49,13,110
	(b) Deferred Tax Liability	44,90,03,570	34,36,49,988	10,53,53,582
	(c) Long Term Provisions	3,43,37,849	1,75,72,110	1,67,65,739
		161,55,91,363	125,85,58,932	35,70,32,431
3	Current Liabilities			
	(a) Short Term Borrowings	72,74,74,160	67,41,11,470	5,33,62,690
	(b) Trade Payables	84,40,28,452	31,81,58,015	52,58,70,437
	(c) Other Current Liabilities	40,37,40,210	29,05,96,578	11,31,43,632
	(d) Short Term Provisions	2,90,10,739	2,63,64,476	26,46,263
		200,42,53,561	130,92,30,539	69,50,23,022
	Total	656,34,59,755	482,95,69,160	173,38,90,595
II	ASSETS			
1	Non-Current Assets			
	(a) Fixed Assets			
	(i) Tangible Assets	369,94,94,737	295,93,32,078	74,01,62,659
	(ii) Intangible Assets	40,22,728	40,22,728	-
	(iii) Capital Work In Progress	12,79,89,147	10,18,01,085	2,61,88,062
	(b) Non-Current Investments	21,26,89,680	21,22,79,000	4,10,680
	(c) Long Term Loans & Adv.	4,37,40,401	2,87,93,422	1,49,46,979
		408,79,36,693	306,62,28,313	78,17,08,380
2	Current Assets			
	(a) Inventories	112,68,36,919	70,84,81,041	41,83,55,878
	(b) Trade Receivables	61,08,76,598	21,21,30,532	39,87,46,066
	(c) Cash and Bank Balances	15,08,23,871	12,54,06,385	2,54,17,486
	(d) Short Term Loans & Adv.	22,51,97,598	17,63,53,273	4,88,44,325
	(e) Other Current Assets	36,17,88,076	30,09,69,616	6,08,18,460
		247,55,23,062	152,33,40,847	95,21,82,215
	Total	656,34,59,755	482,95,69,160	173,38,90,595



8.2 Note on adjustments considered and not considered:

8.2.1 Contingent liabilities in the nature of tax disputes were not reduced from the value of the undertakings and value has been arrived based only on the liabilities which are already accounted. This is because the management is of the opinion that outflow of resources regarding these contingencies is unlikely. The contingent liabilities related to the Demerged Undertaking are as follows:

Particulars	Semi-Regulated (Rs.)
Income Tax Appeals	22,62,309
Income Tax-Interest	1,02,23,132
Central Excise (Interest)	82,87,763
Total	2,07,73,203

8.2.2 No assets and liabilities are revalued and book value as available in financial statements is considered for valuation

8.3 **Value Conclusion:** From the above workings, the Regulated Business is valued at **Rs.226,17,79,689/-** and the Semi-Regulated Business is valued at **Rs.68,18,35,142/-**

9. Limitations and Disclaimer

- 9.1 We have relied upon the information, data and explanations detailed in paragraphs above, for the purpose of reporting on the value of the Regulated Business and Semi-Regulated Business in connection with the proposed demerger.
- 9.2 For the purpose of arriving at the value, we have used financial and other information provided by the Management, which we believe to be reliable and decisions/recommendations of Audit Committee communicated vide letter dated 08-08-2016, our conclusions are dependent on such information being complete and accurate in all material respects. Our scope of work does not enable us to accept responsibility for the accuracy and completeness of the financial and other information provided to us by the Management. We have, therefore, not carried out any due diligence review, independent audit or other test or validation of such financial and other information to establish the accuracy or sufficiency of the financial statements referred to above or of the information, explanations and representations provided to us. We have thus relied upon the audit, carried out by the statutory auditors, of the financials of SMS Pharma provided to us. Accordingly, we do not express any opinion or any other form of assurance thereon and accept no responsibility for the same.
- 9.3 The Semi-Regulated Business of SMS Pharma is proposed to be demerged into the Resulting Company with effect from the Appointed Date and we have considered the



financial statements of SMS Pharma and carved out financial statements of the Semi-Regulated Business as at 31st March, 2016. The Management has explained that the Business would be carried on in due course of business from the Appointed Date and subsequently, till the Scheme is approved. The Management has represented that financial statements of SMS Pharma and the carved out financial statement of the Semi-Regulated Business as at 31st March, 2016, provided to us, include all disclosures necessary for a fair presentation of its financial position and results of operations in accordance with generally accepted accounting principles in India consistently applied, and disclosures otherwise required by the laws and regulations to which they are subject.

- 9.4 Our scope of work is limited to reporting the value of the Regulated Business and Semi-Regulated Business. Our report is not, nor should it be construed as, our opining or certifying the compliance of the proposed demerger of the Demerged Undertaking with the provisions of any law including Companies Act, FEMA and taxation related laws etc., or as regards any legal implications or issues arising from such proposed demerger.
- 9.5 The fee for this engagement is not contingent upon the results of the Valuation Report.
- 9.6 We understand that the equity shares of the Resulting Company shall be listed on any stock exchange and the shareholders of SMS Pharma are being provided shares as provided in the Scheme of De-merger. We are not required to comment on listing of the equity shares of SMS Lifesciences and the fairness / adequacy of the exit option being provided to the shareholders to whom shares cannot be issued.
- 9.7 Determination of Value is not a precise science and the conclusions arrived at in many cases will, of necessity, be subjective and dependent on the exercise of individual judgement. There is, therefore, no indisputable single value of a company. While we have provided our view on the value of the Regulated Business and Semi-Regulated Business based on the information available to us and within the scope and constraints of our engagement, others may have a different opinion.
- 9.8 We owe responsibility to only the Board of Directors of the Companies which has appointed us, and nobody else. We do not accept any liability to any third party in relation to the issue of this Report. This Report is not a substitute for the third party's own due diligence/ appraisal/ enquiries/ independent advice that the third party should undertake for his purpose. It is understood that this analysis does not represent a fairness opinion. The report is confidential and has been prepared exclusively for the Client namely, SMS Pharmaceuticals Limited. It should not be used or relied upon by, reproduced or circulated to any other person or for any purpose other than as mentioned above, in whole or in part, without the prior written consent of the Valuers. Such consent will only be given after full consideration of the circumstances at the time. We will not accept any responsibility or liability to third parties to whom our report may be shown or into whose hands it may come without our prior written consent.
- 9.9 Neither all nor any part of the contents of this report shall be disseminated to the public through advertising, public relations, news, sales or other media without our prior written consent.

