Equity Research

EUROFINANCE
MEMBER OF EUROHOLD

Regulated by the Bulgarian FSC

SOPHARMA AD — SELL — March 4th, 2010

Sector: **HEALTHCARE**	ISIN	BG11SOSOBT18	Last price	BGN 4.02
Industry: **PHARMACEUTICALS**	BSE (XETRA)	3JR	52-week change	+120.9%
www.sopharma.bg	BLOOMBERG	3JR.BU	Market cap	BGN 530.64 mn
	REUTERS	SFARM.BB	P/E (ttm)	11.13
	Index	SOFIX, BG40, BGTR30	P/Book (mrq)	1.84

**** Fixed exchange rate BGN 1 = € 0.51129***

"SAFE HEAVEN" IN TIMES OF PRESSURE

Summary:

- SOPHARMA incorporates 16 companies operating in the field of pharmacy, including pharmaceutical plants located in Bulgaria, Russia, Serbia, Ukraine and Poland, Bulgaria #1 drug wholesaler, REITs, etc.
- SOPHARMA is the biggest Bulgarian pharmaceutical producer. The company has a strong position on the local generic market.
- SOPHARMA exports 64% of its drug production. The group wholesaler Sopharma Trading supplies 22% of the local pharmaceutical market. Medicines production and wholesaler business have equal weights in the group revenue structure.
- SOPHARMA is an active M&A player in Bulgaria and Eastern Europe. For the period 2001 – 2009 SOPHARMA acquired 17 companies. Currently the merger of two local publicly traded subsidiaries is awaiting approval from the FSC.
- For the year 2009 SOPHARMA is expected to generate revenue of almost BGN 500.0 mn and net profit of about BGN 49.0 mn. According to the forecast EBITDA margin will reach 15% up from 10% in 2008.
- During the last years SOPHARMA maintained stable dividend policy. Along with the measures taken against the economic slump, in 2009 for the first time SOPHARMA retained all of its net profit in order to accumulate significant cash exposure in seeking for the next M&A target.
- SOPHARMA shares are listed on the BSE-Sofia. SOPHARMA is a component of all three BSE indices – SOFIX, BG40 and BGTR30. The company is included in Dow Jones STOXX EU Enlarged Total Market Index, Dow Jones STOXX Balkan 50 Equal Weighted Index and MSCI Europe Pharmaceuticals.
- Shares of SOPHARMA are included in Erste Bank Bulgaria Basket certificate, CECE MID certificate (Vienna Stock Exchange), Raiffeisen Osteuropa Fonds and ABN AMRO SOFIX-Open-end-certificate.
- SOPHARMA clearly declared its intentions to list its shares on the Warsaw Stock Exchange and has an approved prospectus for admission to trading on regulated markets in EU. Warsaw listing is one step closer after the Polish Central Depository and Unicredit Bulbank signed a custodian agreement, which will implement the connection between the two countries' depositories.

Source: Bloomberg

Prepared by:

Desislava Petrovska
Financial analysts

Disclaimers

Persons who have prepared this equity research ***do not own*** stocks in the Company or stock in the Company's direct competitors. All views expressed in this research represent personal opinion only. No part of the compensation of these persons was, or will be, directly or indirectly, related to the specific recommendations or views they have expressed in the research.

The present research has been drawn up by EUROFINANCE together with its affiliates, as indicated on the cover page hereof.

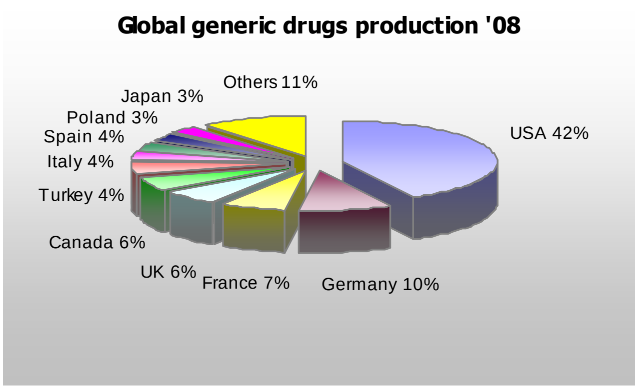
continued on last page

INSIDE THIS ISSUE

1. Pharmaceutical Market and Competitive Environment

During the recent years pharmaceutical market and especially generics market has been changing. The industry has been experiencing high growth rates in both turnover and profits. Companies have striven to increase market share and protect profit margins by using available funds to acquire other firms. The growth of generic drugs producers was fueled by the patent expirations of branded medicines held by the major drug players. At the same time the number of consumers, who welcome the availability of cheaper drugs that can do the job of the "blockbuster drugs", constantly rise. Additional factors that contribute to the growth of generic industry are reforms falling under drug regulations in the US and Europe, cost-containment, new generic entrants, etc.

Generic drugs are very popular because they save both the patients and health-insurance companies substantial costs. When a particular drug-maker loses patent, competition intensifies because all other producers are able to produce the same drug. They sell it at lower cost and yet maintain profitability. Originator companies also reduce prices of off-patent originator medicines in an attempt to fight generic drugs competition. Thus additional savings to patients are generated.

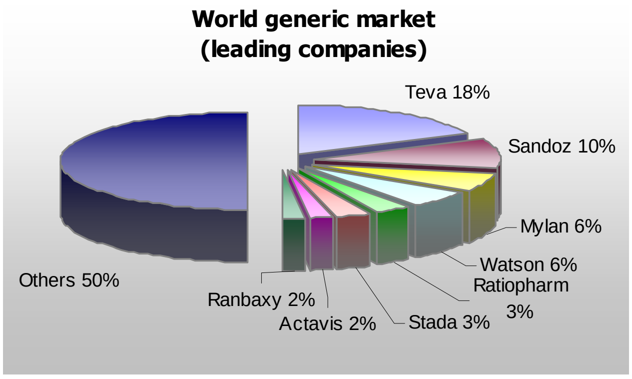


Generic drugs provide patients with safe, effective, high-quality medicines at 20% - 80% of the price of the branded originator medicines. These drugs support the sustainability of healthcare provision and contribute to pharmaceutical expenditures control. Two years after entering the market, generic drugs are 40% cheaper than the originals.

In 2008 the global market of generic drugs was estimated at $80 bn and this figure is expected to reach $84 bn in 2009 (BCC Research). The 5-year annual growth rate is projected at 9%. According to these estimations the market is expected to amount to $129 bn till 2014.

Generics currently dominate the US, which is estimated at $34 bn in 2009. The expected compound annual growth rate is 9.7%. According to BSS forecasts the US market will reach $54 bn in 2014.

The leading companies, which share the world generic market, are Teva (Israel), Sandoz (Germany), Mylan (USA) and Watson (USA). The following figure represents their share in the global generic market in 2008:



During the years European generic drug environment has experienced dramatic changes. Generic companies became increasingly international due to the more complex business situation. Companies have to collaborate with governments to create the best possible conditions for developing, manufacturing and marketing of their products. European generics market is fragmented in accordance with the differences in social standards and development. The EU has attempted to bring a measure of consistency to the market, which is not so easy. Member states have individual regimes adapted to their individual economic and healthcare needs, with a complex pricing, regulation and reimbursement regime. European generic drugs market is estimated at €30 bn. According to the European Generic medicines Association (EGA) the patents on 90 molecules in medicines with European sales, worth nearly €60 mn, expired in 2009. In spite of the positive global trends, the market entering of generic drugs in Europe slows down and there is a slump in the number of new medicines that reached the market. The expiries will rise to a peak of 110 molecules in 2012, worth more than €90 bn.

Generic drugs are expected to account for 60% of the pharmaceutical market in CEE, which was worth €17.2 bn in 2008. Generic drugs market is expected to achieve 14% annual growth in the next three years, which is weigh above the innovative drugs CAGR. Most of the CEE pharmaceutical companies are generic-oriented. The biggest markets are Russia, Poland, Czech Republic and Ukraine. Russia has the necessary potential to be one of the biggest markets in the world due to its numerous population. Romania and Serbia also have the ambitions to be among the top markets. Situation in Poland is not very different from the situation in Russia. Population also contributes for the market volume of about $5.4 mn. Generic drugs have the leading share in the number of medicines that the state reimburses to patients.

According to Standard & Poor's in 2009 branded drug sales were set to decline for the first time due to the increasing competition from generics. According to IMS Health this year $24 bn worth of branded drugs will get generic competitors, up from $18bn last year and the figure is forecasted to hit $30 bn by the end of 2012.

Important industry trends:

- ✓ Generic drugs will capture a larger share of the global drugs market in the future.
- ✓ According to estimates, the sales of brand name drugs will face increasing competition from generics in 2012.
- ✓ Generic industry benefits form the efforts to increase the generic substitution rates in order to save money for consumers and governments.
- ✓ Consolidation of small and mid-sized companies by the big industry players will continue.
- ✓ In 2009 the patents of many blockbuster drugs expired.
- ✓ Aging population and rising healthcare costs incite generics consumption.

Sopharma AD represents 7% of the local Bulgarian market and is the second largest pharmaceutical company in terms of market share, right after the Bulgarian unit of Actavis. Despite its wide product range of over 270 medical products, Actavis is not a direct competitor of Sopharma AD due to the differences of their assortments. On the domestic market Sopharma competes with about 200 producers and importers of medicines.

BULGARIAN PHARMACEUTICAL MARKET BY PRODUCERS, 2008

Producer	Market share
Actavis	9%
Sopharma	**7%**
Novartis	6%
Servier	5%
Glaxosmithkline	5%
Sanofi-Aventis	4%
Menarini	4%
Roch	3%
Novo Nordisk	3%
Bayer	3%
Pfizer	3%
Thaikapharma	3%
Gedeon Richter	2%
Astra Zeneca	2%
KRKA	2%
Zentiva	2%
Others	37%
TOTAL	**100%**

source: Sopharma AD, Annual Report 2008

On the international market Sopharma faces competition mainly from generic companies from India, which record impressive growth and are significantly larger than the Bulgarian pharmaceutical group.

2. SOPHARMA Overview

"Sopharma pharmaceuticals" produces and trades with medical products, cosmetics and pharmaceutical substances. Production activity of Sopharma group includes:

- Medical products
- Substances and preparations based on vegetable materials (photochemical production)
- Veterinary vaccines
- Infusion solutions
- Amorphous silica
- Sodium silicate solution
- Medical products for humane and veterinary medicine
- Injection-moulded and blow-moulded articles for the household, industry and agriculture

Sopharma production comprises wide range of medical forms - tablets, ampoules, lyophil forms (concentrates), syrups, unguents, droppers, suppositories and others. The company is the only Bulgarian producer of ampoules and suppositories and is the leading supplier of these products on the domestic market. Sopharma has five plants in Bulgaria – ampoule plant, tablet plant, suppositories plant, "Vrabevo" plant for production of solid forms, gels, syrups and unguents and pharmaceuticals substance plant. Ampoule, suppositories and Vrabevo plants operate under the requirements of Good Manufacturing Practices (GMP). In 2010 a new highly technological plant for solid forms will be fully operational. The investment amounted to €35 mn. All activities related to the project - construction and validation - are carried out according to the European Standards for pharmaceutical production and are coordinated with the Bulgarian National Drug Agency.

In the following table are presented the major plants of Sopharma and their annual capacity.

TOTAL PRODUCTION CAPACITY

Plant	Location	Annual capacity
Tablet plant	Sofia	2,400 mn tablets
Ampoule plant	Sofia	80-100 mn ampoules
"Vrabevo" plant	VRABEVO village	540 mn tablets, 14.4 mn syrups, 18 mn unguents
Lyophil products plat	Sofia	7.2 mn ampoules 4.3 mn lyophil ampoules
Chemical products plant	Sofia	720,000 tons of herbs
Suppositories plant	Sofia	2.8 mn packs

Sopharma group owns intellectual property, including registered rights – brands, patents, designs and unregistered elaborations (technological, production, know – how). These assets are a result of the special group policy towards production and technological renovation.

Product portfolio of Sopharma comprises more than 140 trade names included in different types of medical forms (tablets, ampoules, syrups, suppositories and unguents) and various concentrations of the active ingredient in them. Generic drugs represent about 90% of the trade names and about 35% of the sales. Brand names of generics are registered trademarks of the company. Original products generate more than 60% of the company's sales, although they are only 10% of the trade names. Original products are based on a vegetable extracts produced by own technology. They are protected with trademark, patent or company know-how. Licensed products have insignificant part in the company's sales.

Domestic market has a prevailing share in the sales structure – 77% as of the end of 2008. Production of Sopharma is exported to 32 countries in Europe, Asia, Africa and North America. A big part of the export is directed to Russia, Ukraine, Kazakhstan, Azerbaijan, Belarus. The most exported products are Sopharma's original medical forms - Carsil®, Tempalgin® and Broncholytin®. The interest in Tabex®, Nivalin®, Tribestan®, Phytin® also rises. The following table presents top 10 of the most sold products as of June 30, 2008 and their share in the sale structure.

Drug	Type	Share
Carsil	Original	19%
Tempalgin	Original	15%
Analgin	Generic	8%
Broncholytin	Original	7%
Tabex	Original	4%
Vitamin C	Generic	4%
Nivalin	Original	3%
Vasopren	Generic	3%
Methylprednisolon	Generic	2%
Sedal	Generic	2%
Total		**67%**

source: Sopharma's Procpectus 2008

Domestic market			Foreign markets		
Analgin	Gen.	17%	Carsil	Orig.	30%
Vitamin C	Gen.	9%	Tempalgin	Orig.	23%
Vasopren	Gen.	5%	Broncholytin	Orig.	13%
Methylprednisolon	Gen.	5%	Tabex	Orig.	6%
Antistenocardin	Gen.	4%	Sedal	Gen.	6%
Chlophadon	Gen.	3%	Cinnarizin	Gen.	4%
Amikacin	Gen.	3%	Indometacin	Gen.	4%
Vicetine	Gen.	3%	Nivalin	Orig.	2%
Nivalin	Orig.	3%	Tribestan	Orig.	2%
Buscolysin	Gen.	2%	Spasmalgon	Gen.	1%
Total		**53%**	**Total**		**92%**

Original products presented only in the list above generate about 50% of the total sales. Exported products are mainly original drugs, while on the domestic market generics have the prevailing share.

Sopharma deals with over 30 drug distributors on the local market. The main clients of the group Sopharma are drug wholesalers, pharmacies, hospitals, Bulgarian National Health Insurance Fund (BNHIF) and Ministry of Health. On the domestic market distributor of Sopharma is Sopharma Trading AD – a part of Sopharma group. The company is very active in the tenders of the Ministry of Health and BNHIF. On the foreign markets company works with local distributors. Sopharma has representation offices in Russia, Ukraine, Georgia, Kazakhstan, Poland, China, Serbia, Lithuania and Azerbaijan.

Short history

Sopharma AD started up as a medical products laboratory in 1933, but later grew into a pharmaceutical plant with the name "Galenus", which was the first modern drug plant on the Balkan peninsula. It was nationalized in 1953. For the period 1953 – 2000 Sopharma was the leading Bulgarian medicines producer. In 2000 67% of Sopharma were privatized by Elpharma – a consortium between Unipharm and Electroimpex. Bulgarian pharmaceutical company Unipharm was just privatized at that time by the present CEO of Sopharma Ognian Donev, while Electroimpex was owned by Bulgarian businessman and entrepreneur Borislav Dionisiev.

Ognian Donev is a well-known name in the Bulgarian pharmaceutical industry and is one of the most successful investors in the country. He is a chairman of the board of directors and executive director of Sopharma AD and a board member of Unipharm AD, Sopharma Trading AD, Doverie United Holding AD etc.

Mr. Donev is a vice-president of the German-Bulgarian Trade-Industrial Chamber, deputy-chairman of the Confederation of Employers and Industrialists in Bulgaria and a Chairman of the Bulgarian National Committee of the International Chamber of Commerce.

He is awarded with prizes in the field of industrial management and capital markets.

After privatization Sopharma modernized and increased its production capacities. At present Sopharma is the main unit in the structure of the group "Sopharma pharmaceuticals". As of September 30, 2009 Sopharma owns 16 subsidiaries – 8 in Bulgaria and 8 abroad. Most of them operate in the field of medicine and produce different types of products for medicine and cosmetics or support the main activity.

Bulgarian subsidiaries that are publicly traded companies listed on the Bulgarian Stock Exchange (BSE) are Bulgarian Rose – Sevtopolis AD, Sopharma Trading AD, Momina Krepost AD and Sopharma Buildings REIT.

Sopharma Trading

Sopharma Trading AD was established after the merger of five drug distributors in the end of 2006 – Sanita Trading, Kaliman RT, Global Medical, Consumpharm and Elpharma. At present the company is a leader in pharmaceutical products distribution on the Bulgarian market. The product portfolio comprises over 7,000 products and includes medical products, medical consumables, sanitary products, vitamins, nutritions, cosmetics, medical equipment and articles. Distribution network covers 100% of the country. The company is a local market leader with 22% share in 2008. In the beginning of the year a contract was signed for the takeover of Sopharma Logistica by Sopharma Trading. Sopharma Logistica is a former mass-privatization fund and currently it generated mainly rental income. The takeover awaits approval by the Financial Supervision Commission.

Bulgarian subsidiaries	Stake	Main activity
Elektroncommerce	100 %	Trade, transport and disband of radioactive materials
Sopharma Trading	92 %	Trade with medical products
Pharmalogistica	76 %	Secondary packaging and real estate lending
Biopharmengineering	69 %	Production and trade with infusion solutions
Bulgarian Rose – Sevtopolis	50 %	Production of medical forms
Momina Krepost	47 %	Medical production
Sopharma Buildings REIT	41 %	Real estate
Foreign subsidiaries	**Stake**	**Main activity**
Sopharma USA (USA)	100 %	Trade with pharmaceutical products and nutritions
Sopharma Investments Limited (Cyprus)	100 %	Portfolio management
Vitamini AD (Ukraine)	99 %	Production and trade with pharmaceutical products
Extab Corporation (USA)	80 %	Portfolio management
Sopharma Poland (Poland)	60 %	Public opinion and market surveys
Rostbalkanpharm (Russia)	51 %	Production and trade of medical products
Inacic i Sinovi (Serbia)	51 %	Production and trade with pharmaceutical products
Sopharma Zdrovit AD (Poland)	50 %	R&D in the field of medicine and pharmacy

Bulgarian Rose - Sevtopolis

Bulgarian Rose – Sevtopolis AD is a successor of the state company "Bulgarian Rose" established to produce, trade and export rose products. Currently Bulgarian Rose – Sevtopolis produces and trades with medical forms and substances, perfumery and cosmetics, natural aromatic products. The company has two types of production – pharmaceutical (solid medical forms) and phytochemical (active pharmaceutical substances based on vegetable raw materials). Production of solid medical forms is focused on two production lines, registered under the trademark of Sopharma AD - CARSIL® and TEMPALGIN® - the two most traded products of Sopharma. The company does not have industrial property and operates under contracts for production with Sopharma.

Momina krepost

Momina krepost AD produces a wide range of products for single use intended for various medical fields – surgery, urology, intensive therapy, gynecology, gastroenterology, diagnosis, anesthesiology, pediatrics etc. Products can be divided in two groups - medical devices for single use and products for household and industry. Momina Krepost has a developed distribution network in Bulgaria and abroad. Globally the company sells its products in more than 15 countries. Momina krepost is one of the leading suppliers of medical devices for single use and export mainly syringes in the local region and former Soviet Union. The company took steps to export on the EU markets as well.

3. SWOT Analysis

STRENGTHS AND OPPORTUNITIES

- Company with traditions in the pharmaceutical industry
- Unique for Bulgarian market products and activities
- Modernized or new machines, plant and equipment
- The lowest prices compared to the products of all other companies
- GMP certificate, which guarantees a high quality of production
- Well-developed logistic network and wide distribution network, that covers the whole country
- Strong connection between the companies from the group (synergy)
- Mass advertising campaigns
- Long-term partnerships with clients and suppliers
- Representative offices in nine different countries
- Slightly correlated with the economic cycle
- Integrated production cycle of phytochemical production

WEAKNESSES AND RISKS

- Limited and old product range
- Highly competitive sector
- Vulnerability to substitutes
- Inadequate level and range of drugs included in the positive list of Ministry of Health and reimbursement list of BNHIF
- Highly concentrated sales structure – the five most traded drugs generated more than 50% of the sales
- Frequent changes in regulatory acts determining the drugs price tops
- High dependence of domestic sales on the tenders for state and municipal orders
- Traditional problems of fast-growing companies

4. Financial Overview

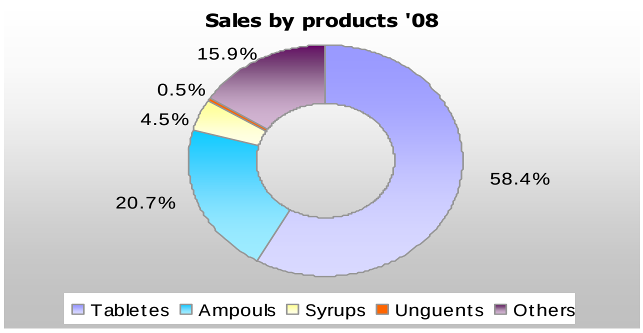
During the recent years Sopharma growth was encouraged by the serious M&A activity that transformed the generic company into a pharmaceutical group. Till 2006 more than 90% of the revenues were generated by the parent company - Sopharma AD, but after consolidation in 2006 of the local drugs distributor Sopharma Trading AD, their share slid to 64%. The following acquisitions of new companies supported this tendency. In 2008 and 2009 subsidiaries generated 63% of the group's sales after consolidation of Momina Krepost AD, Vitamini AD, Ivancic I Sinovi OOD, Sopharma Buildings REIT and Sfarm Investments Limited.

Company's results were not seriously hurt by the global economic downturn, since pharmaceutical sector is not closely correlated to the economic cycle. According to preliminary unaudited 2009 report sales growth shrank to 10.1% y/y from 28% in 2008. Results are highly influenced by the increasing market share of Sopharma Trading along with the growth of the national pharmaceutical market. Sales grew both on the Bulgarian market (9%) and foreign markets (15%). Domestic market has the prevailing share in the structure of sales - 75.5%, dominated by tablet forms, ampoules, syrups and unguents. Sales increased also in the Balkan region, especially Turkey, Caucas, Middle Asia and Baltic states. Cost-cutting program boosted net profit, which more than doubled from BGN 18.2 mn to BGN 47.8 mn. Profitability improved and EBITDA margin reached 13.6% from 10.3% in the end of 2008.

Sopharma group generates its primary income from the sale of own production (manufactured by Sopharma and its affiliates) and trade with imported pharmaceutical products. For the last two years (2008 and 2009) these two income sources have equal weight in the structure of sales. From the sale of own production Sopharma group generated BGN 252.0 mn (preliminary non-consolidated figure) in 2009, compared to BGN 228.7 mn a year ago. The rise of 10.2% in 2009 is due mainly to the strengthening position of the group on the foreign markets. EBITDA margin based only on the sale of own production also improves - from 21% in 2008 to 28% in 2009.

The registered wholesaler of Sopharma pharmaceuticals - Sopharma Trading AD distributes products of the group as well as imported medical products to hospitals and pharmacy chains only in Bulgaria. The share of these sales in the revenue structure is 63% as of the end of 2008. Pharmaceutical production sold on the foreign markets represents 23.5% of the total revenues. The figures presented in this paragraph differ from the officially announced data due to some discrepancies, which arose in consolidation process, for example - according to 2008 consolidated financial report Sopharma registered a 77% drop in its domestic market sales, while on non-consolidated basis the figure is -6%. Since 2008 all production sold on the domestic market is accounted on consolidated basis entirely as goods distributed in Bulgaria. So the figures were recalculated by Euro-Finance in order to reflect fairly the primary revenue sources of the group.

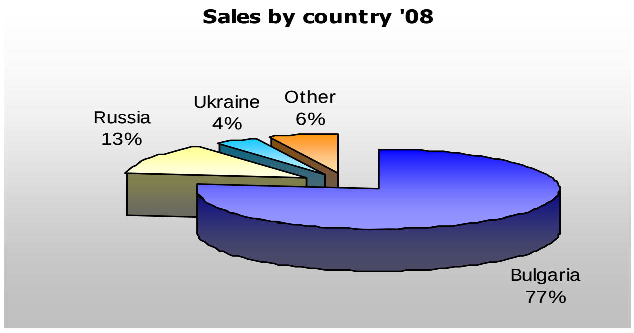
On consolidated basis tablet forms generated more than half of the sales distributed on the local market in 2008, followed by ampoules. Sales of these two product types increased with more than 50% during 2008[1] and boosted domestic sales to BGN 348.4 mn from BGN 265.8 mn a year ago. Tablet forms are the most exported product for the company, followed by syrups and ampoules.



During the recent years the share of export declined on consolidated basis, since the significant turnover growth of the wholesaler Sopharma Trading AD outperformed the growth of the producer Sopharma AD.

Production is exported to 37 countries. Sopharma is oriented towards markets with high growth potential with low healthcare expenses and medicines per capita. In 2008 63.0% of produced drugs are sold abroad. In 2009 this share rose to 65.5%.

Active advertising campaign of Carsil, Tempalgin, Broncholytin, etc. boosted demand for Sopharma's original products and trademarks in Russia. In 2008 Russian drugs market grew with 15%, while Sopharma sales in Russia expanded with significantly higher rate - 29%. Sales in Ukraine were hit by the change of the trade currency from US dollars to euro, which led to higher drug prices. At the same time this change limits company's currency risk exposure. Other markets include Caucas, Baltic countries, Moldova, Mongolia, Albania, Turkey and Macedonia. Tablets have the prevailing share in the structure of foreign sales, followed by syrups.

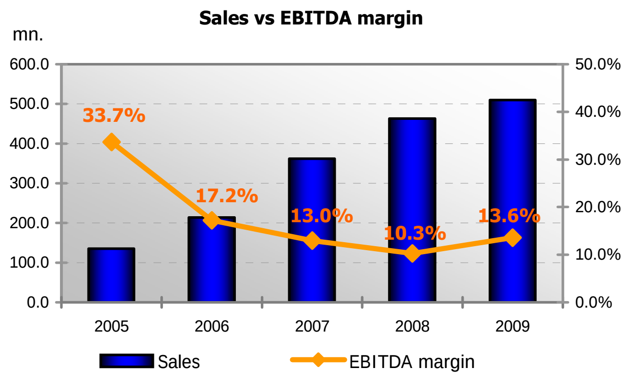


[1] Since Sopharma does not provide balance sheet and income statement notes in its interim reports, the structure of sales is presented as of December 31st 2008

Sopharma made moves to protect its business from the negative impact of the global financial crisis. The serious cost optimization took effect and as of the end of 2009 company's results and ratios considerably improved. Operating expenses rose with only 6%, while sales jumped with 10%. Materials expenses shrank with 11%, mainly as a result of the operating expenses drop in the parent-company.

Although the net profit declined from BGN 31.0 mn in 2005 to BGN 18.2 mn in 2008, as of the end of 2009 it more than doubled to BGN 47.8 mn.

In the period 2005 -2008 EBITDA margin followed downtrend, since the intensive sales growth, mainly as a result of the consolidation of the wholesaler Sopharma Trading, was offset by the higher growth of operating expenses. The negative tendency was terminated in 2009 when the ratio improved to 13.6%.



The serious investments that the company made in the period 2006 – 2008 boosted property, plant and equipment item with BGN 100.1 mn to BGN 187.2 mn. In 2008 company invested BGN 32.4 mn in implementation of a new module for the ampoule production, reconstruction of building, purchase of assembly line, machines for inspection of ampoules, new phytochemical workshop, etc.

For the period 2005 – 2009 assets CAGR is 15.2%. This rise was highly influenced by the current assets CAGR of 21.1%. For the period under review the structure of current assets is changing dynamically.

During 2005 – 2008, when Sopharma Trading was acquired, the growth of inventories was the main driver of the current assets' growth. Inventories increased from BGN 37.9 mn to BGN 111.9 mn. Goods held available in stock in Sopharma Trading generated BGN 56.0 mn of this rise.

In 2009 current assets grew with additional 22.7% or BGN 60.6 mn. In contrast to the previous years, their rise in 2009 was triggered by the expanding receivables. Trade receivables (from hospitals, wholesalers, vaccines) increased with BGN 52 mn, while receivables from related parties added another BGN 12 mn.

Liquidity ratios of Sopharma maintain sound levels. The company accumulated bigger cash in 2009 mirrored by the cash ratio, which rose from 0.06 in 2008 to 0.08. The company added BGN 7.2 mn to its cash and cash equivalents items as a result of the significant advance of the operating cash flow and shrinking capital expenses affected by the economic crisis.

The capital structure of Sopharma changed in favor of debt, but the equity still has the prevailing share. As of December 2009 debt/equity ratio is 0.89. In the period 2005 – 2009 equity/assets ratio is relatively stable and fluctuates in the range 0.50 – 0.58 and as of the end of 2009 is 0.53.

In 2009 interest expenses related to the interest-bearing debt decline from BGN 10.4 mn in 2008 to BGN 7.6 mn, while the debt itself increased with 5%. The average cost of debt in 2009 drops to 4.25% from 6.5% a year ago, since Bulgarian banks bound loans interest rates mainly to the EURIBOR.

After a serious rise during the recent years, some of the Sopharma's long-term bank loans mature in 2010 so the long-term liability amounted to BGN 44.6 mn was transferred to the current debt.

During the recent years net working capital remains stable at around BGN 100 mn unlike the rising revenue. The NWC-to-assets ratio gradually dropped from 0.28 in 2005 to 0.19 in 2009.

5. Valuation

DCF Valuation

Valuation of Sopharma group is based on a 5-year forecast period and comprises the years from 2010 to 2014. Revenue structure consists of three parts in accordance with the income sources:

- *Source 1* - Production and trading with medicines produced by Sopharma group on the Bulgarian market;
- *Source 2* - Production and trading with medicines produced by Sopharma group on the foreign markets;
- *Source 3* - Trading with imported medical products on the Bulgarian market.

Sales on the local market are expected to grow with 4% in 2010 and 7% in 2011. The growth will gradually decline to 5% in 2013 and will stabilize at the level in 2014. Export is forecasted to increase with 15% in 2010 and then gradually decrease to 10% in 2014. The highest growth is expected in 2011 due to the new plant for production of solid forms, which will be operational in the end of 2010. In addition, in the domestic sales structure are included sales of medical equipment and other medical but non-drug products that are not produced by the group. They are fixed at 2% of the revenues. Sales of imported products are forecasted to rise between 10% and 5% in the period 2010 – 2014 and will maintain this level in 2015.

In the total sales structure is included one more item – other sales, fixed at 1.5% of the revenues in every year during the selected period.

Basic model assumptions (%)	2010	2011	2012	2013	2014
Revenues growth, incl.:	10.0	9.5	7.9	7.0	6.5
Source 1	*4.0*	*7.0*	*6.0*	*5.0*	*5.0*
Source 2	*15.0*	*14.0*	*13.0*	*12.0*	*10.0*
Source 3	*10.0*	*8.0*	*6.0*	*5.0*	*5.0*
EBITDA margin	15.0	15.0	15.0	15.0	15.0
Tangible assets growth	10.0	7.0	5.0	5.0	5.0
A&D-to-Revenues	2.7	2.7	2.7	2.7	2.7
NWC-to-Revenues	19.0	18.0	17.0	16.0	15.0

During the period 2006 – 2009 EBITDA margin varied between 10% and 17%. According to preliminary 2009 consolidated report the ratio is 14%, but for the whole forecasted period the ratio is set at 15%.

Weighted-average cost of capital is assumed at 10.8% with cost of equity of 13% and cost of debt of 7%. Debt-to-Equity ratio is calculated taking into account only the interest-bearing debt and is fixed at 0.50 for the whole period.

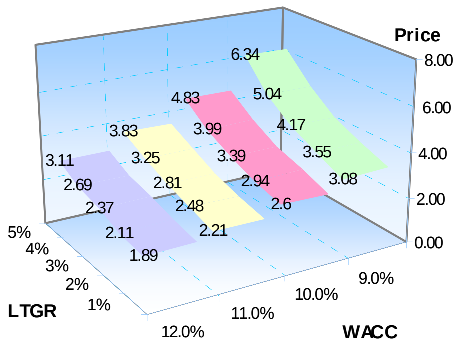
In the calculation of the terminal value we assume 3% long-term growth rate, which corresponds to the expectations for the long-term economic growth including inflation.

According to our DCF valuation net value of Sopharma is BGN 484.5 million (EUR 247.7 mn). This represents an estimated price per share of BGN 3.67.

Since we value Sopharma's share as a minoritary investor, we add a 20% discount from DCF valuation due to the lack of controlling interest over the company, so the price comes to BGN 2.94 per share.

The following chart presents the price per share of Sopharma group according to different levels of weighted average cost of capital and long-term growth rate. The most pessimistic version includes WACC of 12% and long-term growth rate of 1% that gives BGN 1.89 per share or total value of the company of BGN 249.5 mn. In the most optimistic version the price is BGN 6.34 with WACC of 9% and growth rate of 5%. In this case, the total net value of the company amounts to BGN 836.9 mn.

Sensitivity analysis *(including 20% discount)*



PEER GROUP ANALYSIS

Sopharma operates in a very competitive sector. Bulgarian competitors are private companies. In CEE most pharmaceutical companies are generic drugs manufacturers. The largest players are **Gedeon Richter**, **Krka**, **Egis** and **Zentiva**. They are very well-established in the region. Consolidation process made them part of global pharmaceutical companies. Teva gained strong presence in CEE through the acquisition of Barr in 2008, which owned one of the largest local generic producers Croatian **Pliva**.

As of September 30th 2009 earnings per share and sales per share of Sopharma on a TTM basis are 0.25 and 3.61, respectively. Book value per share is 2.01. Using the average values of the three ratios, the price per share of the group is estimated at BGN 4.57. This value should be corrected with liquidity premium since the companies from the peer group are more actively traded on the stock exchanges. The liquidity premium is defined at 10%.

Peers	Country	P/E TTM*	P/S TTM	P/B MRQ*
Krka	Slovenia	14.5	2.3	2.6
Zentiva	CEE	84.4**	1.4	0.9
Pliva	Croatia	-	1.9	1.7
Egis	Hungary	10.2	1.2	1.1
Gedeon Richter	Hungary	14.7	2.9	2.1

** TTM – trailing twelve months; MRQ – most recent quarter*
*** excluded from valuation*

According to the peer group analysis the price for one share of Sopharma is BGN 4.11 or BGN 542.5mn for the whole group.

CONCLUSION

FOR THE TWO METHODS OF VALUATION WERE USED EQUAL WEIGHTS. AS A RESULT WE HAVE REACHED A FAIR VALUE OF SOPHARMA OF BGN 465.1 MN OR BGN 3.52 PER SHARE.

ACCORDING TO OUR ESTIMATE SOPHARMA IS CONSIDERED OVERVALUED. COMPARED TO THE PRESENT PRICE LEVELS THE GROUP IS TRADING WITH A PREMIUM OF 12.4%. DESPITE THE POSITIVE EXPECTATIONS FOR 2009 RESULTS OUR RECOMMENDATION IS *SELL*. SOPHARMA GROUP IS TRADING AT THE AVERAGE LEVEL FOR ITS COMPETITORS, BUT WE THINK THAT LOWER PRICES ARE QUITE POSSIBLE, ESPECIALLY IN CASE OF CONTINUING MARKET DOWNTREND.

6. Key Financials

Income Statement (audited, consolidated)

All figures in BGN million

	2005	2006	2007	2008	2009 (not audited)
Sales	130.1	211.0	357.7	455.5	502.6
Other revenues	5.6	2.4	4.8	7.5	7.1
Total revenue	**135.7**	**213.4**	**362.5**	**463.0**	**509.7**
Change of finished goods and work in progress	5.7	5.2	-1.9	14.9	-1.0
Materials	-49.3	-51.6	-50.5	-72.3	-64.5
External services	-19.4	-25.2	-35.2	-48.8	-48.3
Employees	-20.2	-25.1	-33.7	-46.6	-47.3
Amortization & Depreciation	-7.9	-11.2	-10.1	-12.3	-12.4
Book value of goods sold	-0.5	-70.6	-186.2	-248.8	-266.3
Restored devaluation of assets	-	-	-	-	-
Other operating expenses	-6.3	-9.4	-7.9	-13.8	-13.0
Operating Profit	**37.8**	**25.6**	**36.9**	**35.4**	**57.0**
Interest and other financial revenues/expenses net	0.9	-1.0	-6.1	-14.2	-5.8
Gains on acquisition of subsidiaries	-0.1	5.7	0.3	-	2.0
Gains on associated companies	-	0.4	0.1	-	-
Pre-tax income	**38.6**	**30.7**	**31.3**	**21.1**	**53.2**
Income taxes	-7.6	-3.6	-3.3	-3.0	-5.4
Net profit/loss	**31.0**	**27.1**	**28.0**	**18.2**	**47.8**
Equity owners in the parent company	31.2	26.8	27.7	17.8	45.9
Minority shareholding	-0.2	0.3	0.4	0.4	1.9
EPS for the equity owners in the parent company (BGN)	**0.47**	**0.20**	**0.21**	**0.13**	**0.35**

Balance Sheet (audited, consolidated)

All figures in BGN million

	2005	2006	2007	2008	2009 (not audited)
FIXED ASSETS	**158.1**	**137.8**	**189.7**	**216.0**	**218.7**
Property, plant and equipment	87.1	122.6	144.9	187.2	183.2
Intangible assets	8.3	4.9	2.7	6.8	7.3
Investments for sale	1.8	1.8	26.8	14.6	18.7
Other	60.9	8.5	15.3	7.4	9.5
CURRENT ASSETS	**152.3**	**225.3**	**238.7**	**251.6**	**327.7**
Inventories	37.9	81.9	83.2	111.9	115.7
Trade receivables and advances	35.1	86.7	94.1	111.2	163.2
Receivables from related parties	61.1	32.3	14.1	13.9	25.6
Other	6.9	10.6	10.9	4.7	6.1
Cash and cash equivalents	11.3	13.8	36.4	9.9	17.1
TOTAL ASSETS	**310.4**	**363.1**	**428.4**	**467.6**	**546.4**
SHAREHOLDER'S EQUITY	**179.0**	**195.0**	**230.0**	**233.5**	**288.5**
Paid-up capital	66.0	132.0	132.0	132.0	132.0
Repurchased shares	-0.7	-0.3	-	-	-
Reserves	29.9	25.8	35.3	26.7	28.4
Accumulated profit	83.1	31.3	49.6	58.7	102.7
Minority shareholdings	0.7	6.2	13.1	16.1	25.4
Long-term LIABILITIES	**65.1**	**41.2**	**65.6**	**80.9**	**31.5**
Long-term loans	48.6	34.3	60.7	73.6	24.6
Other	16.5	6.9	4.9	7.3	6.9
Current LIABILITIES	**66.3**	**126.9**	**132.8**	**153.2**	**226.3**
Short-term loans	31.9	50.0	76.3	92.3	105.7
Trade liabilities	10.2	58.3	35.2	40.8	54.9
Other	24.2	18.6	21.3	20.1	65.7
TOTAL LIABILITIES	**131.4**	**168.1**	**198.4**	**234.1**	**257.8**
EQUITY AND LIABILITIES	**310.4**	**363.1**	**428.4**	**467.6**	**546.4**

Key ratios

		2005	2006	2007	2008	2009 (not audited)
EBITDA margin	ttm	33.7%	17.2%	13.0%	10.3%	13.6%
Operating profit margin	ttm	27.9%	12.0%	10.2%	7.6%	11.2%
Net profit margin	ttm	22.9%	12.7%	7.7%	3.9%	9.4%
ROaA	ttm	11.1%	8.0%	7.1%	4.1%	9.4%
ROaE	ttm	18.2%	14.5%	13.2%	7.8%	18.3%
Current ratio	mrq	2.30	1.78	1.80	1.64	1.45
Quick ratio	mrq	1.72	1.13	1.17	0.91	0.94
Cash ratio	mrq	0.17	0.11	0.27	0.06	0.08
Leverage	mrq	1.73	1.86	1.86	2.00	1.89
Debt-to-Equity ratio	mrq	0.73	0.86	0.86	1.00	0.89
Equity / Assets	mrq	0.58	0.54	0.54	0.50	0.53
Current Liabilities / Equity	mrq	0.37	0.65	0.58	0.66	0.78

This analysis has been prepared as investment research pursuant to article 42, para. 6 of Ordinance No. 38 of 25 July, 2007 on the requirements to the activities of investment intermediaries, in accordance with legal requirements designed to ensure the independence of investment research.

This investment research has been drawn up and approved for free dissemination by Euro-Finance for its own goals and for the needs of its clients and, if requested, shall be submitted to them on hard copy.

Prior to publication this research has been approved by the head of Euro-Finance's Internal control department.

By no means, this analysis constitutes a recommendation or offer for the purchase or sale of securities. The information and opinions contained in this research are based upon information available to the public at the time of preparation and publication. The factual statements herein have been taken from sources we consider reliable, but such statements are made without any representation as to the accuracy or completeness or otherwise.

This analysis has been prepared by Euro-Finance with due care and to the best of our knowledge, the research does not contain incorrect, misleading or incomplete data.

This publication and any recommendation contained herein speak only as of the date hereof and are subject to change without notice.

Euro-Finance, its affiliates and employees shall have no obligation to update or amend any information or opinion contained herein.

Opinions expressed in this research belong to Euro-Finance, unless otherwise stated.

The value of and income from an individual investment decision may vary because of changes in interest rates, tax rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of the company or other factors.

Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realized.

This research is not individually tailored. It has been prepared with no regard to the individual financial circumstances and objectives of persons who receive it. The securities discussed in this research may not be suitable for all investors.

This research is intended for investors who are able to thoroughly evaluate and accept potential risks to an investment in shares issued by this company.

Euro-Finance recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser.

This document should not be interpreted as providing of an investment service as per the meaning of Article 5, para. 2 of Markets of Financial Instruments Act.

Investing in publicly traded securities including equities involves significant risks such as fluctuation of exchange rates that may have adverse effects on the value or price of income derived from the security.

Securities of some companies at times may be less liquid and prices more volatile than securities of other companies.

Euro-Finance and/or its directors and employees or any other person related to them by affinity have or may have small positions in securities mentioned in this research (or in any related investment), may from time to time add to or dispose of any such securities, or may execute transactions in these securities that may not be consistent with the conclusions of this research.

No Euro-Finance's employee or member of its management body is at the same employee or member of management body of the company covered by this research.

As of the date of the preparation of this research Euro-Finance does not own any shares of the company covered by this research.

This investment research, nor any part of it, has been, or will be, shared with, or communicated to the subject company prior to its publication.

Neither this corporate profile (analysis) nor any part of it has been prepared on the basis of a contract between Euro-Finance and the issuer and will not be presented to the company, covered by this profile, before its publication.

Euro-Finance does not make a market in the securities covered by this research.

Euro-Finance Ltd. has set up and applied organizational and administrative measures for the prevention and avoidance of conflicts of interest in accordance with the Euro-Finance's Conflicts of Interest Policy, laid down in Euro-Finance's Rules on Internal Organization and Internal Control (in effect as of 2nd of April 2008).

Euro-Finance is not a party under a contract with the issuer for provision of investment services.

Information sources used

THE INFORMATION USED IN THE PREPARATION OF THIS INVESTMENT RESEARCH HAS BEEN TAKEN FROM COMPANY'S PUBLIC FINANCIAL STATEMENTS AND THE RELATED ENCLOSURES, WHICH ARE AVAILABLE ON THE WEB PAGES OF THE BULGARIAN STOCK EXCHANGE - SOFIA – WWW.BSE-SOFIA.BG, THE FINANCIAL SUPERVISION COMMISSION OF THE REPUBLIC OF BULGARIA - WWW.FSC.BG, INFORMATION SYSTEM X3 - WWW.X3NEWS.COM AND THE HOME PAGE OF THE COMPANY, SHOWN ON THE COVER PAGE HEREOF.

IN THE PREPARATION OF THIS RESEARCH EURO-FINANCE HAS USED INFORMATION FROM PUBLICLY DISSEMINATED PRESENTATIONS OF THE COMPANY.

THIS RESEARCH SHALL BE RELEASED ON THE ELECTRONIC PAGE OF EURO-FINANCE LTD. /WWW.EURO-FIN.COM/ FOR THE TERM NOT LESS THAN ONE MONTH AFTER THE DATE OF ITS FIRST PUBLICATION.

Contact us:

www.euro-fin.com

research@euro-fin.com

Tel: +359 2 980 56 57

Fax: +359 2 981 14 96

Mail: Sofia 1540, BULGARIA

43, Hristofor Columbus blvd.

SWIFT: EUFCBGSF

BLOOMBERG page: EUFN