

Sagent Pharmaceuticals

Inline 3Q Results; Next New Product Cycle
Anticipated in 2012

Sagent reported an in-line 3Q/11 with improving gross margin trends due to new product launches and a more favorable product mix, rebounding from a difficult 2Q/11 with gross margins well below expectations. Looking ahead to 4Q/11, we expect relatively few new product introductions for Sagent with accelerating new launches now expected in 2012. While we believe that Sagent is positioning well to take advantage of supply shortages facing the generic injectables industry, we continue to see a fairly balanced risk/reward in SGNT shares at current levels and maintain our Neutral rating.

- **Relatively in-line quarter helped by new launches.** Sagent reported 3Q/11 loss per share of (\$0.17) (-\$0.06 v. JPMe, in line with consensus) on revenue of \$41.3 million (+\$400K v. JPMe and -\$700K v. consensus). Gross margin, which was a key issue in previous quarters, came in slightly below expectations at 16.8% (-69 bps v. JPMe and -120 bps v. consensus) but rebounded nicely from 2Q/11 levels.
- **Six new products launched in the quarter.** Sagent launched six products during 3Q/11 including Zosyn, Gemzar, Taxol, polymyxin B and vecuronium bromide. Taxol (paclitaxel) and vecuronium bromide are both on the FDA drug shortages list. Pricing on Zosyn, which saw unexpected pricing competition from Pfizer this year, is still challenging and the company does not expect the pricing landscape to improve in the near future. On Taxol, Sagent has been able to price its product at a premium to the two other competitors in the market who have both faced supply issues. Like many of the shortage products Sagent is targeting, the company anticipates keeping its price high in exchange for reliable supply that it is providing.
- **New launches help to diversify portfolio; several additional launches expected in early 2012.** We expect a relatively modest 4Q/11 launch profile for SGNT with the company's new product launches expected to accelerate significantly in early 2012 as the company completes several site transfers and gains approvals for additional products. This quarter, no single product accounted for more than 20% of total revenue and 10 products represented 80% of the company's revenue during the quarter, reflecting an increasingly diversified portfolio for the company.

Neutral

SGNT, SGNT US

Price: \$22.25

Price Target: \$25.00

Generic Pharmaceuticals

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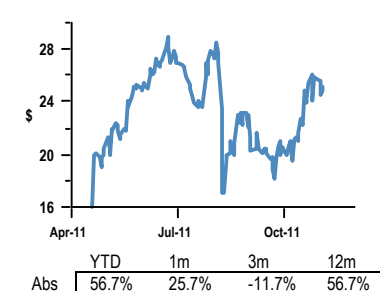
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Price Performance



Sagent Pharmaceuticals, Inc. (SGNT;SGNT US)

FYE Dec	2011E	2011E	2012E	2012E	2013E	2013E	2014E	2015E
	(Prev)	(Curr)	(Prev)	(Curr)	(Prev)	(Curr)		
EPS Reported (\$)								
Q1 (Mar)	(2.09)A	(2.09)A	(0.01)	(0.01)	-	-	-	-
Q2 (Jun)	(0.37)A	(0.37)A	0.05	0.05	-	-	-	-
Q3 (Sep)	(0.11)A	(0.17)A	0.14	0.12	-	-	-	-
Q4 (Dec)	(0.06)	(0.13)	0.23	0.24	-	-	-	-
FY	(0.86)	(1.04)	0.42	0.41	1.70	1.64	2.36	2.68
Bloomberg EPS FY (\$)	(0.85)	(0.85)	0.46	0.46	1.80	1.80	-	-

Source: Company data, Bloomberg, J.P. Morgan estimates.

Company Data

Price (\$)	22.25
Date Of Price	07 Nov 11
52-week Range (\$)	29.23 - 13.50
Mkt Cap (\$ mn)	620.22
Fiscal Year End	Dec
Shares O/S (mn)	28
Price Target (\$)	25.00
Price Target End Date	31 Dec 12

See page 8 for analyst certification and important disclosures.

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- **Adjusting estimates.** We are modestly adjusting estimates following 3Q results. While management does not give specific line item guidance, the company still expects 2011 revenue to be double 2010 revenue and expects gross margins to be in the mid-teens range for 2011. Sagent may issue formal 2012 guidance when the company reports 4Q/11 results early next year.

Changes to Our Estimates

Figure 1: Sagent 3Q/11 Performance v. JPM Estimates

\$ in millions

Sagent	JPM 3Q/11E	Reported 3Q/11A	Variance
Total revenue	\$40.9	\$41.3	\$0.4
Cost of goods sold	\$33.7	\$34.3	\$0.6
Gross profit	\$7.2	\$6.9	(\$0.2)
Gross margin	17.5%	16.8%	-69 bps
SG&A	\$6.3	\$6.7	\$0.4
R&D	\$3.0	\$3.5	\$0.5
Equity in JV	\$0.5	\$0.4	(\$0.1)
Operating income	(\$2.6)	(\$3.6)	(\$1.0)
Operating margin	-6.4%	-8.7%	-234 bps
Interest/other (expense)	(\$0.5)	(\$1.1)	(\$0.6)
EPS	(\$0.11)	(\$0.17)	(\$0.06)
Shares	28.0	27.9	-0.1

Source: Company reports and J.P. Morgan estimates.

Figure 2: Changes to Sagent Revenue and EPS Estimates

Sagent Period	EPS			Revenue (\$ millions)		
	Revised	Prior	Difference	Revised	Prior	Difference
4Q/11E	(\$0.13)	(\$0.06)	(\$0.07)	\$44	\$48	(\$4)
2011E	(\$1.04)	(\$0.86)	(\$0.18)	\$148	\$152	(\$4)
2012E	\$0.41	\$0.42	(\$0.01)	\$246	\$243	\$3
2013E	\$1.64	\$1.70	(\$0.06)	\$340	\$344	(\$4)
2014E	\$2.36	\$2.38	(\$0.02)	\$421	\$424	(\$3)
2015E	\$2.68	\$2.69	(\$0.01)	\$494	\$496	(\$2)

Source: J.P. Morgan estimates.

Investment Thesis

Maintain Neutral rating. We believe Sagent's unique injectable generic model, which combines a network of development and manufacturing partners with a highly experienced sales organization, positions the company well for long-term market share gains and significant top- and bottom-line growth. However, given the company is at a relatively early stage in its development, we believe near-term results could remain volatile and see a fairly balanced risk/reward at current levels.

Valuation

Maintain December 2012 price target of \$25. As Sagent is not yet profitable and with few pure comparisons to Sagent in the generic pharmaceutical universe, we use a DCF methodology to arrive at our December 2012 price target of \$25 for SAGENT shares.

Our DCF considers our estimates through 2015 and then modest revenue growth through 2025, flattening out thereafter. In addition, we expect Sagent's cost structure to remain consistent with 2015 levels. We believe our terminal growth rate of zero (off 2030 estimated cash flow) reflects a long-term strategy of additional product launches and share gains offsetting any normal price erosion in the industry.

We estimate a weighted average cost of capital (WACC) of 10.5%, which is higher than our normal WACC estimates due to the risk in Sagent's business model relative to other more established generics companies. We expect Sagent's WACC will decrease over time as the company continues to build scale in the generics injectables market. We use a long-term estimated tax rate of 30% in our analysis.

Risks to Rating and Price Target

Risks to the downside include production issues working with a large number of suppliers, revenue concentration in a few product areas (Heparin), the critical need for margin expansion to achieve profitability, the reliance on the current management team's expertise and industry connections to continue to gain market share and a large insider hold of SGNT shares.

Risks to the upside include the potential for significant product launches in the near future as the company works to build out its portfolio, continued manufacturing and supply issues for other injectable generic competitors and the potential for revenue-accretive business development transactions.

Figure 3: Sagent Annual Revenue Estimates

\$ in millions

millions USD Fiscal year ends December 31	FY 2008A	FY 2009A	FY 2010A	FY 2011E	FY 2012E	FY 2013E	FY 2014E	FY 2015E
Revenue								
heparin			18.8	37.5	29.6	24.1	19.1	18.1
growth				99%	-21%	-19%	-21%	-5%
piperacillin/tazobactam (Zosyn)			-	4.8	11.2	10.7	10.1	9.6
growth					132%	-5%	-5%	-5%
gemcitabine (Gemzar)			-	9.3	17.1	14.6	13.8	13.1
growth					85%	-15%	-5%	-5%
New products			-	10.0	106.0	212.5	300.0	375.0
growth						100%	41%	25%
Current base business	12.0	29.2	55.2	86.3	82.0	77.9	77.9	77.9
growth		143%	89%	56%	-5%	-5%	0%	0%
TOTAL REVENUE	12.0	29.2	74.1	148.0	245.9	339.7	420.9	493.8
growth		143%	153%	100%	66%	38%	24%	17%

New Product Assumptions
3Q/11 products
growth
4Q/11 products
growth
2011 New Products
growth
1Q/12 products
growth
2Q/12 products
annualized growth
3Q/12 products
annualized growth
4Q/12 products
annualized growth
2012 New Products
growth
2013 products
growth
2014 products
growth
2015 products
growth
Total New Products

8.0	15.5	15.5	15.5	15.5
	94%	0%	0%	0%
2.0	8.0	8.0	8.0	8.0
	300%	0%	0%	0%
10.0	23.5	23.5	23.5	23.5
	0%	0%	0%	0%
	50.0	47.5	47.5	47.5
	0%	-5%	0%	0%
	15.0	19.0	19.0	19.0
	0%	27%	0%	0%
	10.0	19.0	19.0	19.0
	0%	90%	0%	0%
	7.5	28.5	28.5	28.5
	0%	280%	0%	0%
	82.5	114.0	114.0	114.0
	0%	38%	0%	0%
		75.0	112.5	112.5
		0%	50%	0%
			50.0	75.0
			0%	50%
				50.0
				0%
10.0	106.0	212.5	300.0	375.0

Source: Company reports and J.P. Morgan estimates.

Figure 4: Sagent Quarterly Financial Model

\$ in millions

millions USD						Mar 2011	Jun 2011	Sep 2011	Dec 2011					
Fiscal year ends December 31	FY 2006A	FY 2007A	FY 2008A	FY 2009A	FY 2010A	1QA	2QA	3QA	4QE	FY 2011E	FY 2012E	FY 2013E	FY 2014E	FY 2015E
Income Statement														
Net sales	-	0.1	12.0	29.2	74.1	30.3	32.3	41.3	44.1	148.0	245.9	339.7	420.9	493.8
COGS	-	0.1	11.9	28.8	65.0	25.8	29.5	34.3	35.9	125.5	184.6	232.3	275.6	318.9
Gross profit	-	0.0	0.1	0.4	9.0	4.6	2.7	6.9	8.2	22.4	61.4	107.4	145.4	174.9
Research & Development	-	2.5	14.9	12.4	11.2	2.4	2.4	3.5	3.5	11.7	14.0	15.4	16.9	18.6
SG&A	1.7	10.6	15.0	16.7	18.9	5.0	6.5	6.7	6.6	24.8	27.6	30.4	33.4	36.1
Equity in JV	-	0.7	1.1	1.5	1.5	0.7	0.5	0.4	0.5	2.1	2.0	-	(2.0)	(5.0)
Total operating expense	1.7	13.8	31.1	30.6	31.6	8.0	9.4	10.5	10.6	38.6	43.6	45.8	48.3	49.7
Operating income (loss)	(1.7)	(13.8)	(31.0)	(30.1)	(22.6)	(3.4)	(6.6)	(3.6)	(2.5)	(16.1)	17.8	61.7	97.1	125.2
Interest income & other	0.0	0.6	0.5	0.1	0.0	0.0	0.1	0.1	0.1	0.2	0.2	0.5	1.2	2.5
Interest expense	(0.1)	(0.0)	-	(0.5)	(1.1)	(0.5)	(1.2)	(1.2)	(1.2)	(4.2)	(4.4)	(4.1)	(3.4)	(2.7)
Change in value of p/s warrants	-	-	-	-	(0.8)	(0.5)	(0.4)	-	-	(0.8)	-	-	-	-
Income (loss) before taxes	(1.7)	(13.2)	(30.5)	(30.5)	(24.5)	(4.4)	(8.2)	(4.7)	(3.6)	(20.9)	13.6	58.1	94.9	125.0
Income tax	-	-	-	-	-	-	-	-	-	-	(1.4)	(8.7)	(23.7)	(43.7)
NET INCOME	(1.7)	(13.2)	(30.5)	(30.5)	(24.5)	(4.4)	(8.2)	(4.7)	(3.6)	(20.9)	12.2	49.4	71.1	81.2
Adjusted EPS						(2.09)	(0.37)	(0.17)	(0.13)	(1.04)	0.41	1.64	2.36	2.68
Basic shares outstanding						2.1	22.2	27.9	28.0	20.0	28.1	28.1	28.2	28.3
FD shares outstanding						2.1	22.2	27.9	28.0	20.0	30.1	30.1	30.2	30.3
Margins														
Gross margin		37.5%	0.6%	1.5%	12.2%	15.1%	8.5%	16.8%	18.5%	15.2%	25.0%	31.6%	34.5%	35.4%
R&D		nm	124.5%	42.4%	15.2%	7.8%	7.4%	8.4%	7.9%	7.9%	5.7%	4.5%	4.0%	3.8%
SG&A		nm	125.1%	57.1%	25.6%	16.4%	20.1%	16.2%	15.1%	16.7%	11.2%	8.9%	7.9%	7.3%
Equity in JV			9.1%	5.1%	2.0%	2.2%	1.6%	1.0%	1.1%	1.4%	0.8%	0.0%	-0.5%	-1.0%
Opex		nm	258.7%	104.6%	42.7%	26.4%	29.1%	25.6%	24.1%	26.1%	17.7%	13.5%	11.5%	10.1%
Operating margin		nm	-258.1%	-103.1%	-30.5%	-11.3%	-20.5%	-8.7%	-5.6%	-10.9%	7.2%	18.2%	23.1%	25.4%
Pretax margin		nm	-253.7%	-104.5%	-33.1%	-14.4%	-25.4%	-11.5%	-8.2%	-14.1%	5.5%	17.1%	22.5%	25.3%
Tax rate		nm	nm	nm	nm	nm	nm	nm	10.0%	0.0%	10.1%	15.0%	25.0%	35.0%
NET MARGIN		nm	-253.7%	-104.5%	-33.1%	-14.4%	-25.4%	-11.5%	-8.2%	-14.1%	5.5%	17.1%	22.5%	25.3%
Growth Rates														
Sales					153%	251%	205%	94%	31%	100%	66%	38%	24%	17%
COGS					126%	208%	177%	85%	31%	93%	47%	26%	19%	16%
R&D					-10%	-16%	-27%	37%	33%	4%	20%	10%	10%	10%
SG&A					14%	19%	49%	49%	12%	31%	11%	10%	10%	8%
Equity in JV					-1%	55%	58%	89%	1%	42%	-5%	-100%		150%
Opex					3%	8%	18%	46%	18%	22%	13%	5%	6%	3%
Operating income												247%	57%	29%
Pretax income												328%	63%	32%
NET INCOME												305%	44%	14%
EPS												304%	44%	14%

Source: Company reports and J.P. Morgan estimates.

Sagent Pharmaceuticals: Summary of Financials

Income Statement - Annual	FY10A	FY11E	FY12E	FY13E	Income Statement - Quarterly	1Q11A	2Q11A	3Q11A	4Q11E
Revenues	74	148	246	340	Revenues	30A	32A	41A	44
Cost of products sold	65	126	185	232	Cost of products sold	26A	30A	34A	36
Gross profit	9	22	61	107	Gross profit	5A	3A	7A	8
SG&A	19	25	28	30	SG&A	5A	6A	7A	7
R&D	11	12	14	15	R&D	2A	2A	3A	4
Operating Income	32	39	44	46	Operating income	8A	9A	11A	11
Note: EBITDA	(21)	(13)	23	67	Note: EBITDA	(3)A	(6)A	(2)A	(1)
Net interest income / (expense)	(1)	(4)	(4)	(4)	Net interest income / (expense)	(1)A	(1)A	(1)A	(1)
Other income / (expense)	(1)	(1)	0	0	Other income / (expense)	(0)A	(0)A	0A	0
Pretax income	(24)	(21)	14	58	Pretax income	(4)A	(8)A	(5)A	(4)
Income taxes	0	0	(1)	(9)	Income taxes	0A	0A	0A	0
Net income - GAAP	-	-	-	-	Net income - GAAP	-	-	-	-
Net income - recurring	(24)	(21)	12	49	Net income - recurring	(4)A	(8)A	(5)A	(4)
Diluted shares outstanding	-	20	30	30	Diluted shares outstanding	2A	22A	28A	28
EPS - excluding non-recurring	-	(1.04)	0.41	1.64	EPS - excluding non-recurring	(2.09)A	(0.37)A	(0.17)A	(0.13)
EPS - recurring	-	(1.04)	0.41	1.64	EPS - recurring	(2.09)A	(0.37)A	(0.17)A	(0.13)
Balance Sheet and Cash Flow Data	FY10A	FY11E	FY12E	FY13E	Ratio Analysis	FY10A	FY11E	FY12E	FY13E
Cash and cash equivalents	35	34	26	84	Sales growth	-	-	-	-
Accounts receivable	19	34	56	61	EBIT growth	-	-	-	-
Inventories	31	40	58	61	EPS growth	-	-	-	-
Other current assets	6	80	80	80					
Current assets	90	188	219	286	Gross margin	-	-	-	-
PP&E	1	1	2	3	EBIT margin	-	-	-	-
Total assets	119	215	240	304	EBITDA margin	-	-	-	-
					Tax rate	-	-	-	-
Total debt	21	34	34	34	Net margin	-	-	-	-
Total liabilities	58	69	78	81					
Shareholders' equity	61	146	162	223	Debt / EBITDA	-	-	-	-
					Debt / Capital (book)	-	-	-	-
Net income (including charges)	(24)	(21)	14	58	Return on assets (ROA)	-	-	-	-
D&A	1	3	5	5	Return on equity (ROE)	-	-	-	-
Change in working capital	(8)	(23)	(31)	(6)	Return on invested capital (ROIC)	-	-	-	-
Other									
Cash flow from operations	(28)	(36)	(7)	60	Enterprise value / sales	-	-	-	-
					Enterprise value / EBITDA	-	-	-	-
Capex	(0)	(0)	(1)	(2)	Free cash flow yield	-	-	-	-
Free cash flow	(28)	(36)	(8)	58					
Cash flow from investing activities	(7)	(80)	(1)	(2)					
Cash flow from financing activities	62	115	0	0					
Dividends	-	-	-	-					
Dividend yield	-	-	-	-					

Source: Company reports and J.P. Morgan estimates.

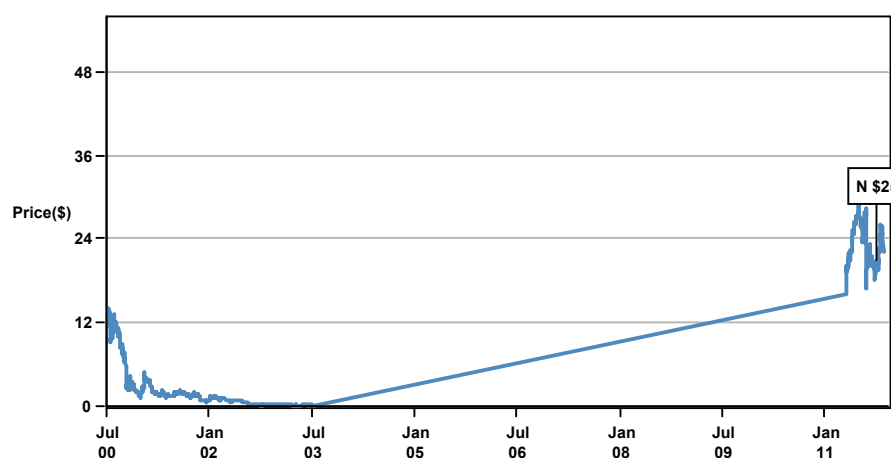
Note: \$ in millions (except per-share data). Fiscal year ends Dec

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- **Market Maker:** JPMS makes a market in the stock of Sagent Pharmaceuticals.

Sagent Pharmaceuticals (SGNT) Price Chart



Date	Rating	Share Price (\$)	Price Target (\$)
28-Sep-11	N	20.96	25.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Sep 28, 2011.

The chart(s) show J.P. Morgan's continuing coverage of the stocks; the current analysts may or may not have covered it over the entire period.

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