

RETAIL EQUITY RESEARCH

Sun Pharmaceutical Industries Ltd

Pharmaceuticals

BSE CODE: 524715

NSE CODE: SUNPHARMA

Bloomberg CODE: SUNP:IN

SENSEX: 31,882

12th September 2017**SELL**

Rating as per Largcap

12months investment period

CMP Rs 469 TARGET Rs 413 RETURN 12%↓

Weak Q1FY18 quarter; pain to continue

Sun Pharma is India's top drug maker and world's fourth largest specialty generic pharmaceutical company by revenue with 42 manufacturing facilities spread across 6 continents. US contributes 37% to the revenues.

- Revenue plunged 25% YoY in Q1FY18 due to lower US and India sales.
- US sales declined 42% YoY mainly on account of sharp fall in Taro sales (down 31% YoY) due to continued pricing pressure in the US and high base impact.
- The domestic formulations business fell by 5% YoY primarily impacted by temporary disruption due to GST implementation.
- EBITDA margin contracted 1760 bps YoY to 17.1% led by lower than expected US and India sales, decline in Taro margin and high base effect. Taro's EBITDA margin fell to 50.5% from 62.6% in Q1FY17.
- We reduce our revenue and PAT estimates for FY18/19E by 16%/14% and 69%/44%, respectively to factor in lower than anticipated growth in the US.
- Given continued pricing pressure in the US generics business due to increased competitive intensity & customer consolidation and delay in Halol plant resolution restricting new launches, we change our rating to 'SELL' from 'BUY' with a revised target price of Rs 413 based on 20x FY19E PE.

Slump in US sales dragged overall consolidated revenue by 25% YoY

Sun Pharma Ltd reported 25% YoY decline in net revenue in Q1FY18 owing to 42% YoY decline in US sales owing to high competitive intensity in the generic drugs market. Moreover, high base last year also impacted the performance. Sales in Q1FY17 were higher due to benefits of 180-day exclusivity for Imatinib which expired in July-2016. Further, dismal numbers from Taro Pharma which reported a sharp decline of 31% in sales due to challenging pricing environment also impacted US performance. India sales also fell 5% YoY impacted by de-stocking ahead of GST implementation. However, Rest of World (ROW) reported steady performance in Q1FY18. Sales in ROW (accounting for around 12% of revenues) grew by 32% YoY partly driven by the revenue consolidation from the acquired brands of Novartis. Further, formulation sales in Emerging markets (accounted for 18% of total sales) rose 5% YoY supported by consolidation of Biosintez acquisition in Russia. During the quarter, the company filed five ANDAs and received eight approvals.

Decline in Taro margin took a toll on overall EBITDA margin

EBITDA margin contracted 1760 bps YoY to 17.1% led by lower than expected US and India sales, decline in Taro margin and high base effect. Taro's EBITDA margin fell to 50.5% from 62.6% in Q1FY17. We lower our EBITDA margin estimates for FY18E and FY19E to 19.9% and 24.4% respectively, to factor in Taro's deteriorating profitability, higher R&D spends and continued price erosion in the US. The improvement in EBITDA margin in FY19E is on account of company's increasing focus on speciality business where it continues to invest to enhance its global speciality and complex generics pipeline. From its speciality pipeline, the company has already launched Bromsite and Odonzo in the US and expects to launch Tildrakizumab (filed in May 2017) along with Seceria in FY19.

Posted net loss due to one-off antitrust litigation charge

Sun Pharma posted net loss in Q1FY18 impacted by a one-off antitrust litigation charge in the US. The company and one of its subsidiaries entered into settlement with plaintiffs in respect of an antitrust lawsuit relating to a sleep-disorder drug Modafinil, whereby the company agreed to pay \$147 million. Excluding the Modafinil settlement, the company's profit stood at Rs 530 crore, down by 74% YoY. We expect Adj. PAT to decline at a CAGR of ~14% over FY17-19E.

Outlook & Valuation

Following a dismal US performance in Q1, we significantly lower US revenue growth rate. We expect US business to decline by 10% CAGR over FY17-19E due to persistent pricing pressure in the US generics business and delay in Halol plant resolution. Uncertainty over Halol plant resolution remains a key overhang on the stock, although, the company has taken remedial measures to address the observations raised by USFDA and awaits approval from the regulator. Despite a disappointing first quarter performance, the company has guided for a single digit decline in revenue for FY18 and expects an expansion in EBITDA margin to 20-22% in H2FY18 as against 17.6% in Q1FY18. We expect revenue to grow at a CAGR of ~1.4% over FY17-19E. However, PAT is expected to decline by 14% CAGR due to weak operating profitability and higher tax outgo. Hence, we change our rating to 'SELL' from 'BUY' with a revised target price of Rs 413 based on 20x FY19E PE.

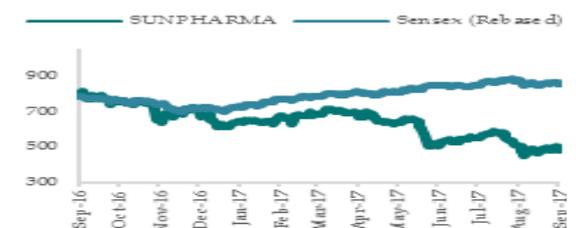
Company Data

Market Cap (Rs cr)	112,443
Enterprise Value (Rs cr)	104,795
Outstanding Shares (cr)	239.9
Free Float	46%
Dividend Yield	0.7
52-week high	Rs818
52-week low	Rs433
6m average volume (cr)	0.5
Beta	1.3
Face value	Rs1

Shareholding %	Q3FY17	Q4FY17	Q1FY18
Promoters	54.4	54.4	54.4
FII's	19.7	21.3	21.8
MFs/Insti	12.9	12.1	12.2
Public	7.3	7.1	6.9
Others	5.7	5.1	4.7
Total	100.0	100.0	100.0

Price Performance	3mth	6mth	1 Year
Absolute Return	(11%)	(32%)	(41%)
Absolute Sensex	2%	10%	11%
Relative Return*	(13%)	(42%)	(52%)

*over or under performance to benchmark index



Consolidated (Rs.cr)	FY17	FY18E	FY19E
Sales	31,310	27,950	32,193
Growth (%)	10.8%	-10.7%	15.2%
EBITDA	9,821	5,563	7,855
Margin (%)	31.4	19.9	24.4
PAT Adj	6,696	3,302	4,957
Growth (%)	24.0	(50.7)	50.1
Adj.EPS	27.9	13.8	20.7
Growth (%)	24.4%	(50.7)	50.1
P/E	16.8	34.1	22.7
P/B	3.1	2.9	2.6
EV/EBITDA	11.1	19.2	13.3
RoE (%)	17.6	7.9	10.9
D/E	0.2	0.1	0.1

Quarterly Financials (Consolidated)

Profit & Loss Account

(Rs cr)	Q1FY18	Q1FY17	YoY Growth %	Q4FY17	QoQ Growth %
Sales	6,209	8,243	(24.7)	7,137	(13.0)
EBITDA	1,096	2,921	(62.5)	1,548	(29.2)
Margin (%)	17.6	35.4	(1,779)	21.7	(404)
Depreciation	347	316	9.7	338	2.5
EBIT	749	2,605	(71.2)	1,209	(38.1)
Interest	109	135	(18.7)	45	143.2
Other Income	152	157	(3.3)	225	(32.3)
Exceptional Items	951	-	-	-	-
PBT	(159)	2,627	(106.0)	1,389	(111.4)
Tax	162	353	(54.1)	44	265.2
PAT	(321)	2,275	(114.1)	1,345	(123.9)
Minority Interest	(104)	(241)	(56.8)	(121)	(13.7)
Reported PAT	(425)	2,033	(120.9)	1,224	(134.7)
Adjustment	(951)	-	-	-	-
Adj PAT	526	2,033	(74.2)	1,224	(57.1)
No. of shares (cr)	239.9	240.7	(0.3)	239.9	-
EPS (Rs)	2.2	8.4	(74.1)	5.1	(57.1)

Business performance

(Rs cr)	Q1FY18	Q1FY17	YoY Growth %	Q4FY17	QoQ Growth %
US	2,265	4,071	(44.4)	2,555	(11.4)
India	1,761	1,854	(5.0)	1,916	(8.1)
Emerging Market (EM)	1,080	1,031	4.8	1,213	(11.0)
RoW	742	563	31.8	732	1.4
Total Formulations	5,848	7,519	(22.2)	6,416	(8.9)
APIs	309	470	(34.3)	396	(22.0)
Others	10	18	(44.4)	14	(28.6)
Total sales	6,167	8,007	(23.0)	6,825	(9.6)

Source: Company, Geojit Research

Change in estimates

Year / Rs cr	Old estimates		New estimates		Change %	
	FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Revenue	33,410	37,356	27,950	32,193	(16.3)	(13.8)
EBITDA	11,256	12,772	5,563	7,855	(50.6)	(38.5)
Margins (%)	33.7	34.2	19.9	24.4	(1380 bps)	(980 bps)
PAT	7,541	8,894	2,351	4,957	(68.8)	(44.3)
EPS	31.4	37.1	13.8	20.7	(56.1)	(44.2)

Source: Company, Geojit Research

Consolidated Financials

Profit & Loss Account

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
Sales	27,580	28,270	31,310	27,950	32,193
% change	71.5%	2.5%	10.8%	-10.7%	15.2%
EBITDA	8,014	8,324	9,821	5,563	7,855
% change	14.5%	3.9%	18.0%	-43.4%	41.2%
Depreciation	1,195	1,014	1,265	1,399	1,497
EBIT	6,819	7,310	8,556	4,163	6,358
Interest	579	477	400	292	233
Other Income	518	617	623	625	675
PBT	6,758	7,450	8,780	4,497	6,799
% change	-4.8%	10.3%	17.8%	-48.8%	51.2%
Tax	915	935	1,212	675	1,224
Tax Rate (%)	13.5%	12.5%	13.8%	15.0%	18.0%
Reported PAT	4,656	4,716	6,696	2,351	4,957
Adj*	238	685	-	951	-
Adj PAT	4,894	5,401	6,696	3,302	4,957
% change	-13.5%	10.4%	24.0%	-50.7%	50.1%
No. of shares (cr)	241	241	240	240	240
Adj EPS (Rs)	20.3	22.4	27.9	13.8	20.7
% change	-25.5%	10.3%	24.4%	-50.7%	50.1%
DPS (Rs)	3.0	1.0	3.5	3.5	3.5

Balance Sheet

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
Cash	10,998	13,989	15,141	16,106	17,600
Accounts Receivable	5,312	6,796	7,203	6,567	7,574
Inventories	5,668	6,424	6,833	6,924	7,844
Other Cur. Assets	5,026	2,941	3,547	3,552	3,847
Investments	2,716	1,309	1,192	1,192	1,192
Gross Fixed Assets	17,213	19,571	22,142	23,743	25,343
Net Fixed Assets	9,488	10,833	12,139	12,341	12,444
CWIP	1,532	2,527	2,801	3,400	4,000
Intangible Assets	3,701	4,181	5,536	5,536	5,536
Def. Tax (Net)	1,752	2,126	2,178	2,178	2,178
Other Assets	2,736	3,032	4,526	4,526	4,526
Total Assets	48,929	54,158	61,095	62,322	66,741
Current Liabilities	8,728	8,026	11,232	11,744	12,796
Provisions	-	-	-	-	-
Debt Funds	8,994	8,338	8,091	5,991	4,791
Other Liabilities	2,719	2,303	1,342	1,342	1,342
Equity Capital	241	241	240	240	240
Reserves and Surplus	25,397	31,164	36,400	38,694	42,643
Shareholder's Fund	25,638	31,405	36,640	38,934	42,883
Minority Interest	2,851	4,085	3,791	4,311	4,930
Total Liabilities	48,929	54,158	61,095	62,322	66,741
BVPS (Rs.)	106.6	130.5	152.7	162.3	178.7

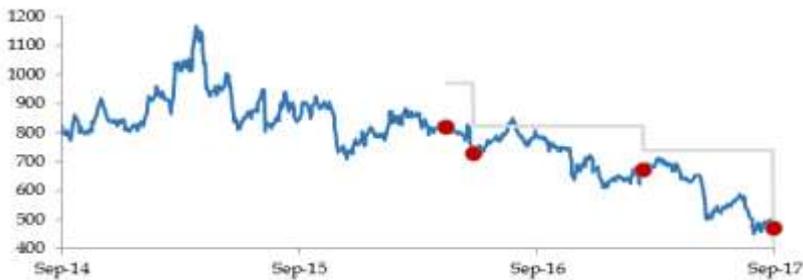
Cash flow

Y.E March (Rs cr)	FY15	FY16	FY17	FY18E	FY19E
Pre-tax profit	6,403	6,765	8,780	4,497	6,799
Depreciation	1,195	1,014	1,265	1,399	1,497
Changes in W.C	(39)	266	(724)	1,051	(1,171)
Others	(496)	713	(223)	(333)	(442)
Tax Paid	(1,740)	(1,988)	(1,212)	(675)	(1,224)
C.F.O	5,322	6,769	7,886	5,939	5,460
Capital exp.	(2,366)	(3,382)	(2,844)	(2,200)	(2,200)
Change in inv.	39	1,552	117	-	-
Other invest.CF	(344)	(2,625)	623	625	675
C.F - investing	(2,671)	(4,455)	(2,105)	(1,575)	(1,525)
Issue of equity	-	9	(1)	-	-
Issue/repay debt	(548)	(782)	(247)	(2,100)	(1,200)
Dividends paid	(363)	(918)	(1,008)	(1,008)	(1,008)
Other finance.CF	(176)	(233)	(3,642)	(292)	(233)
C.F - Financing	(1,087)	(1,924)	(4,898)	(3,399)	(2,441)
Chg. in cash	1,563	390	884	965	1,494
Closing cash	10,998	13,989	15,141	16,106	17,600

Ratios

Y.E March	FY15	FY16	FY17	FY18E	FY19E
Profitab. & Return					
EBITDA margin (%)	29.1	29.4	31.4	19.9	24.4
EBIT margin (%)	26.6	28.0	29.3	17.1	21.8
Net profit mgn.(%)	17.7	19.1	21.4	11.8	15.4
ROE (%)	20.0	16.9	17.6	7.9	10.9
ROCE (%)	24.3	19.5	19.9	9.8	13.8
W.C & Liquidity					
Receivables (days)	70.0	88.6	86.9	86.9	86.9
Inventory (days)	307.0	361.6	306.7	308.0	306.6
Payables (days)	58.8	63.9	74.7	74.1	74.2
Current ratio (x)	3.1	3.8	2.9	2.8	2.9
Quick ratio (x)	2.4	3.0	2.3	2.2	2.3
Turnover &Levg.					
Gross asset T.O (x)	2.1	1.5	1.4	1.2	1.3
Total asset T.O (x)	0.7	0.5	0.5	0.4	0.5
Int. covge. ratio (x)	11.8	15.3	21.4	14.3	27.3
Adj. debt/equity (x)	0.3	0.2	0.2	0.1	0.1
Valuation ratios					
EV/Sales (x)	4.1	4.0	3.6	3.9	3.3
EV/EBITDA (x)	14.2	13.4	11.1	19.2	13.3
P/E (x)	23.0	20.9	16.8	34.1	22.7
P/BV (x)	4.4	3.6	3.1	2.9	2.6

Recommendation Summary (last 3 years)



Source: Bloomberg, Geojit Research

Dates	Rating	Target
25-April-16	BUY	970
06-June-17	BUY	823
23-February-17	BUY	741
12-September-17	SELL	413

Investment Rating Criteria

Large Cap Stocks;		Mid Cap and Small Cap;			
Buy	-	Upside is 10% or more.	Buy	-	Upside is 15% or more.
Hold	-	Upside or downside is less than 10%.	Accumulate*	-	Upside between 10% - 15%.
Reduce	-	Downside is 10% or more.	Hold	-	Absolute returns between 0% - 10%.
			Reduce/Sell	-	Absolute returns less than 0%.
To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.					

The recommendations are based on 12 month horizon, unless otherwise specified. The investment ratings are on absolute positive/negative return basis. It is possible that due to volatile price fluctuation in the near to medium term, there could be a temporary mismatch to rating.

* For reasons of valuations/return/lack of clarity/event we may revisit rating at appropriate time. Please note that the stock always carries the risk of being upgraded to BUY or downgraded to a HOLD, REDUCE or SELL.

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