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Pharmaceuticals  
SUNP IN  
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## The slower uptake of specialty launches to restrict the margin expansion going forward.

RATING	NEUTRAL
CMP	417
Price Target	413
Potential Upside	-1%
Rating Change	↔
Estimate Change	↔
Target Change	↓

STOCK INFO	
52wk Range H/L	679/350
Mkt Capital (Rs Cr)	100062
Free float (%)	46%
Avg. Vol 1M (,000)	7181
No. of Shares (Crs)	240
Promoters Pledged %	11%

### 1QFY20 Result Update

- The overall sales for the quarter grew by 16% YoY to Rs. 8374 crs (vs. our estimate of Rs. 8355 crs) driven by one-off supply opportunity and Pola pharma consolidation .
- India Sales grew by 8% YoY to Rs.2314 crs. The adjusted India sales growth excluding the impact of change in distribution for India business was 12% YoY for the quarter.
- US sales grew by 12% YoY to US\$ 424 mn; sales for the quarter include the contribution from a significant business of generic supply to a customer.
- Taro posted Q1FY20 sales of US\$ 161 million, up 4% over Q1FY19. Taro's net profit for Q1 was US\$ 66 million, marginally down over Q1FY19.
- ROW sales grew by 56% to US\$ 167 mn on account of both organic initiatives as well as consolidation of Pola Pharma (Japan) business.
- R&D spends for the quarter was at Rs.422 crs (5.1% of sales) compared to Rs.500 crs (7% of sales) in Q1FY19. Going forward, the R&D expenses are expected to increase.

### View and Valuation

Overall revenue for the quarter grew by 16% YoY Rs.8374 crs. India sales grew by 8% YoY to Rs. 2314 crs, the underlying growth was 12%, excluding the impact of change in distribution for India business. The US sales grew by 12% YoY to US\$424 mn the driven by significant business of generic supply to a customer. Taro posted sales of US\$ 161 million this quarter, up 4% over Q1FY19. ROW sales grew by 56% to US\$ 167 mn on account of integration of Pola Pharma business. The gross margin declined by 20 bps to 70.7% on account of product mix across geographies and the India distribution transition.

Going forward, we don't expect to see a huge traction in the US revenues on account of slower uptake in the specialty products and lack of one-off supply opportunity. The higher promotional, marketing and the R&D expenses in the coming quarters will restrict the margin expansion. Therefore, we value the stock at 20x FY21e EPS to arrive at a target price of Rs.413 and recommend NEUTRAL.

### Key Risks to our rating and target

- Higher promotional expenses
- Specialty ramp up
- R&D expenditure

### RESEARCH ANALYST

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Fig in Rs Cr

KEY FINANCIAL/VALUATIONS	FY17	FY18	FY19	FY20E	FY21E
Net Sales	31578	26489	29066	32553	34623
EBITDA	10089	5608	6308	7274	7963
EBIT	8825	4108	4554	5359	5991
PAT	6964	2162	2666	4334	4958
EPS (Rs)	29	9	11	18	21
EPS growth (%)	54%	-69%	23%	63%	14%
ROE (%)	19.0%	5.7%	6.4%	9.6%	10.0%
ROCE (%)	23.2%	10.3%	10.6%	11.5%	11.7%
BV	153	159	173	188	207
P/B (X)	4.5	3.1	2.8	2.2	2.0
P/E (x)	23.7	55.0	43.1	23.1	20.2

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## 1QFY20 Results

Fig in Rs Cr

FINANCIALS	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	YoY %	QoQ%	FY18	FY19	YoY %
Net Sales	7,224	6,938	7,740	7,164	8,374	15.9%	16.9%	26,489	29,066	9.7%
Other Income	200	351	193	282	213	6.6%	-24.3%	839	1,025	22.3%
COGS	2,107	1,758	2,166	1,839	2,458	16.7%	33.7%	7,425	7,869	6.0%
Gross Margin	71%	75%	72%	74%	71%	-0.2%	-3.7%	72%	73%	1.0%
Employee Cost	1,433	1,470	1,495	1,569	1,540	7.5%	-1.8%	5,367	5,967	11.2%
Other Expen.	2,078	2,178	1,927	2,740	2,381	14.6%	-13.1%	8,090	8,922	10.3%
EBITDA	1,607	1,531	2,153	1,017	1,996	24.2%	96.3%	5,608	6,308	12.5%
EBITDA Mar.	22%	22%	28%	14%	24%	1.6%	9.6%	21%	22%	0.5%
Depreciation	402	427	471	454	457	13.8%	0.7%	1,500	1,753	16.9%
EBIT	1,205	1,105	1,682	563	1,538	28%	173.4%	4,108	4,554	10.9%
Interest	131	130	145	150	104	-21%	-30.6%	518	555	7.3%
PBT	1,274	1,326	1,730	694	1,647	29.3%	137.3%	4,429	5,025	13%
Exceptional Item	-	1,214	-	-	-	-	-	951	1,214	28%
Tax	164	219	271	(29)	146	-10.9%	-607%	845	601	-29%
PAT	983	(219)	1,240	636	1,387	41.2%	118%	2,162	2,666	23%
PAT Margin	14%	-3%	16%	9%	17%	3.0%	8%	8%	9%	1%

### One-off supply opportunity and Pola pharma consolidation drives sales growth this quarter.

The overall sales for the quarter grew by 16% YoY to Rs. 8374 crs (vs. our estimate of Rs. 8355 crs). The growth was mainly driven by US one-off supply opportunity and consolidation of Pola Pharma. The domestic sales normalized this quarter post India distribution transition and grew by 8% YoY to Rs. 2314 crs. US sales excluding Taro grew by 17% YoY to US\$ 263 mn on account of one - off supply opportunity this quarter, Q1FY20 being the last quarter for the supply opportunity to be serviced; we do not see traction in the US revenues going ahead. Taro posted Q1FY20 sales of US\$ 161 mn, up 4% over Q1FY19. ROW business grew by 56% to US\$ 167 mn on account of both organic initiatives as well as consolidation of Pola Pharma (Japan) business.

### Higher promotional expenses for specialty products to impact margin expansion

The company has committed around US\$ 1 billion to build the specialty business in the US by the way of acquisitions over the years. It has launched 3 products in FY19. However, the growths of these products are slow and rather sticky as it is dependent on the promotional activities. Therefore, the slower uptake in revenues and higher promotional expenses will continue to put pressure on margins in the medium term.

### Update on the specialty launches:

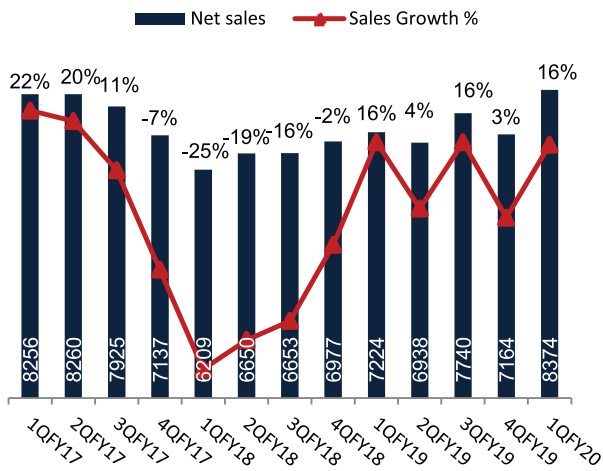
- The specialty sales for the quarter were at US\$ 94 mn across all market. The R&D spends for specialty was 15% of the total R&D expenses.
- Odomzo- Market share has improved slightly to 12%.
- Illumya- The product is gradually ramping up, the company will continue to spend on promotion to increase its prescription counts.
- Cequa - The Company expects to launch the product in Q3FY20. The launch got delayed on account of supply chain and manufacturing challenges.

### Concall Highlights

- For the quarter, 3 ANDAs were filed and 13 approvals were received.
- R&D spends for the quarter was at Rs.422 crs (5.1% of sales) compared to Rs.500 crs (7% of sales) in Q1FY19. Going forward, the R&D expenses are expected to increase.
- The specialty sales for the quarter were at US\$ 94 mn across all market. The R&D spends for specialty was 15% of the total R&D expenses.
- Other expenses were higher by 15% YoY on account of increased Promotional expenses and the consolidation of Pola Pharma.
- Update on specialty products:
- Illumya- The product is gradually ramping up, the company will continue to spend on promotion to increase its prescription counts.
- Cequa - The Company expects to launch the product in Q3FY20. The launch got delayed on account of supply chain and manufacturing challenges.
- Odomzo- The market share of the product is currently 12%.
- Tax rate is expected to see an increasing trend in the coming quarters.

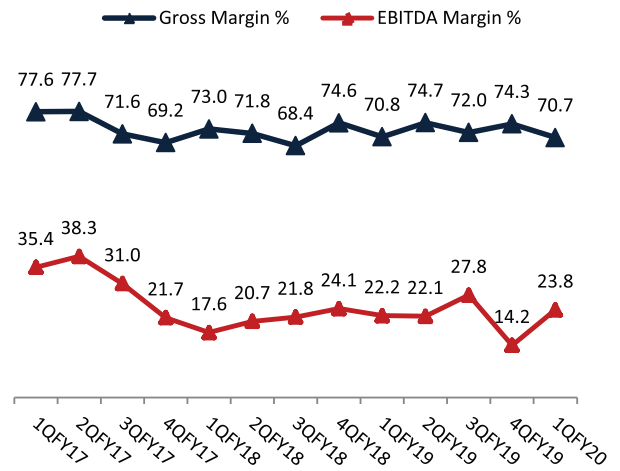
## Exhibit: Net sales and Sales Growth

Sales for the quarter grew by 16% YoY to Rs.8372 crs (vs our expectation of Rs. 8355 crs)



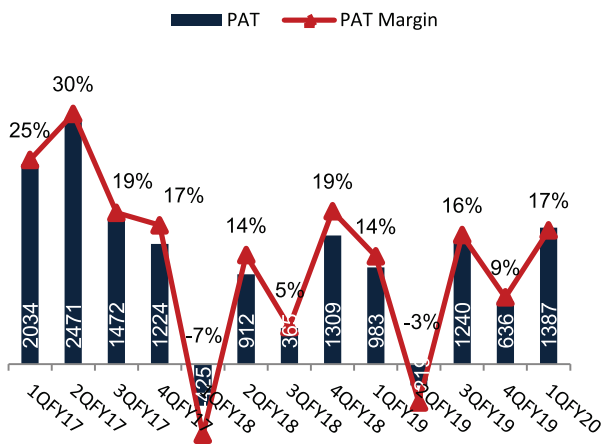
## Exhibit: Gross and EBITDA margin

Gross margin declined by 20 bps to 70.7% on account of product mix and the India distribution transition.



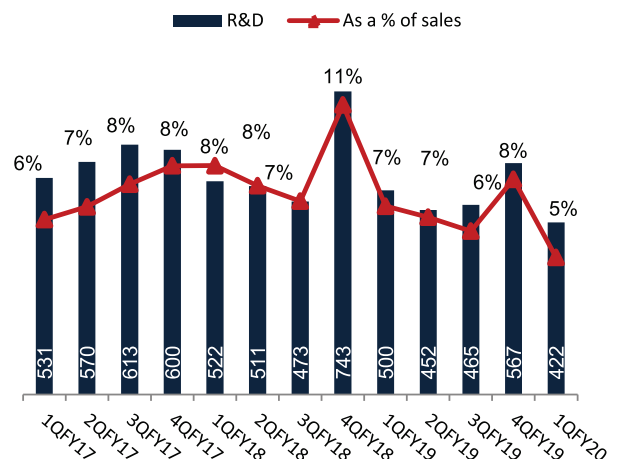
## Exhibit: PAT and PAT margin

PAT for Q1FY20 grew by 41% YoY to Rs. 1387 crs. PAT margin was at 17%.



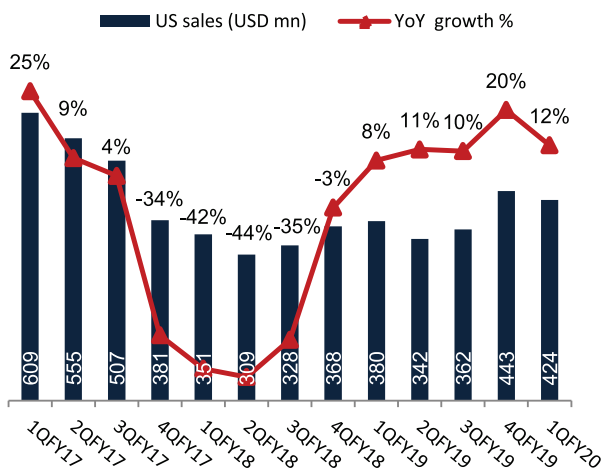
## Exhibit: R&D cost and R&D as a % of sales

R&D spends for the quarter was at Rs.422 crs (5.1% of sales) compared to Rs.500 crs (7% of sales) in Q1FY19.



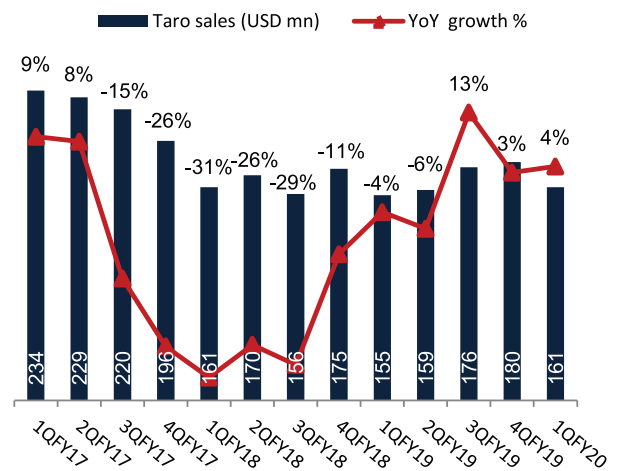
## Exhibit: US sales and YoY growth%

US sales grew by 12% YoY to US\$ 424 million. Ex of Taro, the revenue grew by 17% YoY to US\$ 263 mn.



## Exhibit: Taro sales and YoY growth%

Taro sales grew by 4% YoY to US\$ 161 mn. Net profit for Q1FY20 was US\$ 66 mn, marginally down over Q1FY19.



## Operational Details

GEOGRAPHY	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Cigarettes	1761	2221	2085	1963	2152	1860	2235	1101	2314
Others FMCG	2265	1986	2124	2372	2544	2398	2606	3190	2942
Agri Business	1080	1258	1221	1279	1309	1372	1462	1246	1346
Paperboards, Paper & Packaging	742	711	777	744	718	762	898	1102	1159
Hotels	309	388	370	332	394	426	426	484	461
Total	10	25	21	21	22	29	30	42	37

REVENUE GR. %	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
India Formulations	-5%	11%	6%	2%	22%	-16%	7%	-44%	8%
US Formulations	-44%	-47%	-38%	-7%	12%	21%	23%	34%	16%
Emerging Market	5%	12%	5%	5%	21%	9%	20%	-3%	3%
ROW Formulations	32%	35%	2%	2%	-3%	7%	16%	48%	61%
API	-34%	6%	1%	-16%	28%	10%	15%	46%	17%
Others	-48%	460%	144%	54%	136%	16%	39%	97%	65%

REVENUE MIX%	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
India Formulations	29%	34%	32%	29%	30%	27%	29%	15%	28%
US Formulations	37%	30%	32%	35%	36%	35%	34%	45%	36%
Emerging Market	18%	19%	19%	19%	18%	20%	19%	17%	16%
ROW Formulations	12%	11%	12%	11%	10%	11%	12%	15%	14%
API	5%	6%	6%	5%	6%	6%	6%	7%	6%
Others	0%	0%	0%	0%	0%	0%	0%	1%	0%

ANDA PIPELINE	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
ANDA filings	8	4	4	19	3	4	5	9	3
ANDA approvals	5	3	5	5	6	4	10	12	13

## Financial Details

### Balance Sheet

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	207	207	241	240	240	240	240	240
Reserves	18,318	25,383	32,742	36,400	37,861	41,169	44,926	49,307
<b>Networth</b>	<b>18,525</b>	<b>25,590</b>	<b>32,982</b>	<b>36,640</b>	<b>38,101</b>	<b>41,409</b>	<b>45,166</b>	<b>49,546</b>
Debt	2,489	7,596	8,316	8,091	9,752	9,893	8,893	7,893
Minority interest	1,921	2,885	4,085	3,791	3,884	3,314	3,314	3,314
Other Non Current Liab	2,886	2,794	2,208	1,657	682	1,109	1,293	1,324
<b>Total Capital Employed</b>	<b>21,014</b>	<b>33,186</b>	<b>41,299</b>	<b>44,731</b>	<b>47,852</b>	<b>51,302</b>	<b>54,059</b>	<b>57,440</b>
Net Fixed Assets (incl CWIP)	7,659	14,721	18,048	20,477	21,318	23,248	23,651	23,951
Non Current Investments	788	599	1,116	961	3,052	3,952	3,952	3,952
Other Non Current Assets	2,238	4,563	6,425	7,019	8,297	6,425	6,586	6,617
<b>Non Current Assets</b>	<b>10,684</b>	<b>19,883</b>	<b>25,589</b>	<b>28,457</b>	<b>32,667</b>	<b>33,625</b>	<b>34,189</b>	<b>34,519</b>
Inventory	3,123	5,668	6,423	6,833	6,881	7,886	8,949	9,518
Debtors	2,200	5,106	6,776	7,203	7,815	8,884	10,082	10,723
Cash & Bank	7,590	10,998	13,182	15,141	9,929	7,276	10,583	12,800
Other Current Assets	5,773	7,144	3,561	3,777	7,011	7,023	7,458	7,746
<b>Current Assets</b>	<b>18,686</b>	<b>28,916</b>	<b>29,941</b>	<b>32,954</b>	<b>31,636</b>	<b>31,069</b>	<b>37,072</b>	<b>40,787</b>
Creditors	1,328	3,287	3,583	4,395	4,766	4,148	4,707	5,006
Provisions	1,961	4,353	2,973	4,016	5,110	2,932	5,788	5,997
Other Current Liabilities	260	2,280	1,381	2,821	2,009	1,889	2,100	2,225
<b>Curr Liabilities</b>	<b>3,549</b>	<b>9,919</b>	<b>7,938</b>	<b>11,232</b>	<b>11,885</b>	<b>8,969</b>	<b>12,596</b>	<b>13,229</b>
<b>Net Current Assets</b>	<b>15,137</b>	<b>18,997</b>	<b>22,003</b>	<b>21,722</b>	<b>19,751</b>	<b>22,100</b>	<b>24,477</b>	<b>27,558</b>
<b>Total Assets</b>	<b>29,371</b>	<b>48,799</b>	<b>55,530</b>	<b>61,410</b>	<b>64,303</b>	<b>64,694</b>	<b>71,261</b>	<b>75,306</b>

### Income Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
<b>Revenue from Operation</b>	<b>16,080</b>	<b>27,392</b>	<b>28,487</b>	<b>31,578</b>	<b>26,489</b>	<b>28,686</b>	<b>32,199</b>	<b>34,280</b>
Change (%)	42%	70%	4%	11%	-16%	8%	12%	6%
<b>EBITDA</b>	<b>7000</b>	<b>7867</b>	<b>8158</b>	<b>10089</b>	<b>5608</b>	<b>6308</b>	<b>7274</b>	<b>7963</b>
Change (%)	43%	12%	4%	24%	-44%	12%	15%	9%
Margin (%)	43.5%	28.7%	28.6%	31.9%	21.2%	21.7%	22.3%	23.0%
Depr & Amor.	409	1195	1038	1265	1500	1753	1915	1972
<b>EBIT</b>	<b>6591</b>	<b>6672</b>	<b>7121</b>	<b>8825</b>	<b>4108</b>	<b>4554</b>	<b>5359</b>	<b>5991</b>
Int. & other fin. Cost	44	579	523	400	518	555	400	395
Other Income	552	548	658	623	839	1,025	908	1,228
<b>EBT</b>	<b>7,099</b>	<b>6,641</b>	<b>7,256</b>	<b>9,048</b>	<b>4,429</b>	<b>5,025</b>	<b>5,867</b>	<b>6,825</b>
Exp Item	2,517	238	685	-	951	1,214	-	-
Tax	702	915	914	1,212	845	601	989	1,365
Minority Int & P/L share of Ass.	738	924	1,114	892	421	541	541	499
Reported PAT	3,879	5,488	5,657	7,836	2,634	3,210	4,878	5,460
<b>Adjusted PAT</b>	<b>3,141</b>	<b>4,539</b>	<b>4,546</b>	<b>6,964</b>	<b>2,162</b>	<b>2,666</b>	<b>4,334</b>	<b>4,958</b>
Change (%)	5%	44%	0%	53%	-69%	23%	63%	14%
Margin(%)	19.5%	16.6%	16.0%	22.1%	8.2%	9.2%	13.3%	14.3%

## Financial Details

### Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	17.0%	17.7%	13.8%	19.0%	5.7%	6.4%	9.6%	10.0%
ROCE	35.5%	24.7%	19.7%	23.2%	10.3%	10.6%	11.5%	11.7%
Asset Turnover	0.5	0.6	0.5	0.5	0.4	0.4	0.5	0.5
Debtor Days	50	68	87	83	108	113	113	113
Inv Days	71	76	82	79	95	100	100	100
Payable Days	30	44	46	51	66	53	53	53
Int Coverage	149	12	14	22	8	8	13	15
P/E	37.9	46.7	43.4	23.7	55.0	43.1	23.1	20.2
Price / Book Value	6.4	8.3	6.0	4.5	3.1	2.8	2.2	2.0
EV/EBITDA	16	26	24	16	20	17	13	11
FCF per Share	15	16	14	15	8	(4)	22	17
Div Yield	0.4%	0.1%	0.4%	0.1%	0.7%	0.4%	0.5%	0.5%

### Cash Flow Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	4,581	6,403	6,571	9,048	3,479	3,810	5,323	6,323
(inc)/Dec in Working Capital	207	180	247	(409)	(212)	(2,696)	956	(863)
Non Cash Op Exp	409	1,195	1,038	1,265	1,500	1,753	1,915	1,972
Int Paid (+)	44	579	523	400	518	555	400	395
Tax Paid	(789)	(1,740)	(1,988)	(2,057)	(742)	(886)	(989)	(1,365)
others	(494)	(1,000)	296	(1,164)	(635)	(340)	-	-
<b>CF from Op. Activities</b>	<b>3,959</b>	<b>5,616</b>	<b>6,686</b>	<b>7,082</b>	<b>3,907</b>	<b>2,196</b>	<b>7,605</b>	<b>6,462</b>
(inc)/Dec in FA & CWIP	(906)	(2,342)	(3,404)	(3,693)	(1,961)	(3,213)	(2,318)	(2,272)
Free Cashflow								
(Pur)/Sale of Inv	(80)	39	1,520	363	(5,594)	31,994	-	-
others	(1,381)	(563)	(2,488)	(892)	4,184	2,720	(2)	(1)
<b>CF from Inv. Activities</b>	<b>(2,367)</b>	<b>(2,866)</b>	<b>(4,372)</b>	<b>(4,222)</b>	<b>(3,371)</b>	<b>(681)</b>	<b>(2,320)</b>	<b>(2,273)</b>
inc/(dec) in NW	(1,140)	75	(38)	(2,732)	(675)	(608)	-	-
inc/(dec) in Debt	2,275	(548)	(678)	1,072	588	(237)	(1,000)	(1,000)
Int. Paid	(23)	(350)	(301)	(334)	(477)	(461)	(400)	(395)
Div Paid (inc tax)	(606)	(363)	(871)	(292)	(976)	(1,424)	(578)	(578)
others								
<b>CF from Fin. Activities</b>	<b>507</b>	<b>(1,187)</b>	<b>(1,889)</b>	<b>(2,285)</b>	<b>(1,539)</b>	<b>(2,731)</b>	<b>(1,978)</b>	<b>(1,972)</b>
Inc(Dec) in Cash	2,099	1,563	426	575	(1,003)	(1,215)	3,308	2,217
<b>Add: Opening Balance</b>	<b>2,260</b>	<b>5,722</b>	<b>7,606</b>	<b>8,067</b>	<b>8,909</b>	<b>8,278</b>	<b>7,276</b>	<b>10,583</b>
Closing Balance	4,359	7,286	8,032	8,642	7,906	7,062	10,583	12,800



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