

Industry
Bloomberg
BSE CODE

Pharmaceuticals
ARBP IN
524804

RATING	NEUTRAL
CMP	425
Price Target	591
Potential Upside	39%

Rating Change	↔
Estimate Change	↔
Target Change	↔

STOCK INFO	
52wk Range H/L	838/390
Mkt Capital (Rs Cr)	24905
Free float (%)	48%
Avg. Vol 1M (,000)	6070
No. of Shares (Crs)	59
Promoters Pledged %	4%

RESEARCH ANALYST

J MADHAVI

j.madhavi@narnolia.com
+91-22-62701222

Q2 growth driven by US & Europe business, regulatory headwinds to persist.

2QFY20 Result update

- Overall revenue grew by 18% YoY to Rs. 5600 crs (vs our estimate of Rs.5596 crs) on account of growth in US and Europe markets.
- The US sales grew by 27% to US\$ 404 mn on account of robust growth in the Injectables business. Aurobindo USA, the company marketing the oral products in the US witnessed a growth of 14% YoY in Q2FY20. Auromedics (Injectables) witnessed a growth of 49% YoY to US\$ 79 million.
- Europe formulations revenue increased by 21% YoY to Rs 1,401 crs, Growth Markets revenue witnessed a growth of 4% YoY to Rs. 319 crs, ARV business declined marginally by 3% YoY to Rs. 238 crs and API revenue decreased marginally by 1% YoY to Rs 806 crs.
- Gross margin grew by 70 bps YoY to 57.7% on account of favorable product and geographical mix, though EBITDA margin shrank 75 bps YoY to 20.8% due to higher staff cost and other expenses.
- Adjusting for the forex loss of Rs.27.2 crs, the PAT grew by 9% YoY to Rs. 667 crs (vs our estimate of Rs. 698 crs).

View and Valuation

The overall revenue grew by 18% YoY to Rs.5600 (vs our estimate of 5596 crs) in Q2FY20 on account of robust growth in the US and the Europe business. The US growth came in majorly on account of robust growth of 49% YoY seen in the injectables business. For Europe, the contribution from the Apotex business led to the revenue growth of 26% YoY to 1401 crs.

The delay in the closure of the Sandoz transaction along with the regulatory headwinds that the company is facing makes us cautious about the stock going forward. The recent 14 observation received by the company for Unit IV (Injectables & Ophthalmics) constitutes 31% of the pending approvals. The injectables business has been one of the key growth drivers in recent times growing 49% YoY this quarter, so the compliance issue in unit IV raises our concern. However, we have largely maintained our estimates for FY21; going forward as things unfold, we will update our estimates accordingly. Therefore, considering these headwinds we remain NEUTRAL on the stock and maintain a target price of Rs. 591 (12x FY21E EPS).

Key Risks to our rating and target

- OAI status in two of its facilities and a warning letter for one.
- 14 483s for Unit IV (31% of the pending approvals).

Fig in Rs Cr

KEY FINANCIAL/VALUATIONS	FY17	FY18	FY19	FY20E	FY21E
Net Sales	15090	16500	19564	22609	24352
EBITDA	3434	3772	3892	4745	4992
EBIT	3007	3214	3224	3781	3927
PAT	2302	2423	2365	2720	2885
EPS (Rs)	39	41	40	46	49
EPS growth (%)	14%	5%	-2%	15%	6%
ROE (%)	24.6%	20.7%	17.0%	16.5%	15.0%
ROCE (%)	31.5%	26.5%	22.9%	22.7%	20.3%
BV	160	199	237	281	327
P/B (X)	4.2	2.8	3.3	1.5	1.3
P/E (x)	17.2	13.5	19.5	9.2	8.6

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2QFY20 Results

Fig in Rs Cr

FINANCIALS	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	YoY %	QoQ%	FY18	FY19	YoY %
Net Sales	4,751	5,270	5,292	5,445	5,600	17.9%	2.9%	16,500	19,564	18.6%
Other Income	26	64	32	16	(7)	-	-	102	116	13.4%
COGS	2,043	2,390	2,373	2,299	2,368	15.9%	3.0%	6,753	8,713	29.0%
Gross Margin	57%	55%	55%	58%	58%	0.7%	-0.1%	59%	55%	-3.6%
Employee Cost	625	650	713	780	777	24.3%	-0.3%	2,131	2,585	21.3%
Other Expen.	1,057	1,144	1,149	1,220	1,288	21.8%	5.6%	3,845	4,374	13.8%
EBITDA	1,026	1,086	1,057	1,146	1,167	13.8%	1.8%	3,772	3,892	3.2%
EBITDA Mar.	22%	21%	20%	21%	21%	-0.7%	-0.2%	23%	20%	-3.0%
Depreciation	164	163	187	241	243	48.6%	1.0%	558	668	19.7%
EBIT	862	923	871	906	924	7%	2.1%	3,214	3,224	0.3%
Interest	35	48	50	50	41	16%	-17.9%	78	163	109.3%
PBT	853	939	853	871	877	2.7%	0.6%	3,238	3,177	-2%
Exceptional Item	27	25	36	13	13	-52.5%	0.5%			
Tax	175	205	231	228	224	27.9%	-1.5%	818	727	-11%
PAT	611	712	585	636	640	4.6%	1%	2,423	2,365	-2%
PAT Margin	13%	14%	11%	12%	11%	-1.4%	0%	15%	12%	-3%

Concall Highlights

- The US sales grew by 27% to US\$ 404 mn on account of robust growth in the Injectables business. Aurobindo USA, the company marketing the oral products in the US witnessed a growth of 14% YoY in Q2FY20. Auromedics (Injectables) witnessed a growth of 49% YoY to US\$ 79 million.
- The company filed 20 products (2-Injectables, 18 Non-Injectables) in the quarter, and received approval for 3 non-injectables.
- The company has launched 10 products including 3 injectables (some oncology products launch from Eugia plant) during the quarter.
- For the sartans, out of 8 sartans, the company right now is present in only two i.e., Losartan and Telmisartan. For the other Sartans, the company is awaiting CB-30 approvals, after which the company will re-launch.
- For Losartan, the company has maintained its market share and it is contributing nicely to the sales.
- Sandoz deal- the FTC consent is expected to be received in the next few weeks.
- Europe formulations revenue increased by 21% YoY to Rs 1,401 crs, Growth Markets revenue witnessed a growth of 4% YoY to Rs. 319 crs, ARV business declined marginally by 3% YoY to Rs. 238 crs and API revenue decreased marginally by 1% YoY to Rs 806 crs.
- For Europe, Ex-Apotex, the growth has been around 6% YoY and along with Apotex, the Europe business has grown by 26% YoY this quarter.
- Europe- the Company is launching new products in Poland and Czech Republic and is also streamlining its operations in Spain and Netherland. There are 200+ products under development.
- Biosimilars is progressing well, 1 product is in Phase1, which has been started for Australia and New Zealand. By the next year, 2 Phase1 and 2 Phase111 are expected to start.
- On the regulatory front, the Company will respond to the USFDA for Unit 11(Warning letters), Unit 1 (OAI) and Unit 9 (OAI) on 15 Nov 2019. Post the submission of the response, the company expects the inspections to be by March to April 2020.
- For Unit 7, the responses have been submitted to the USFDA and the plant is under review.
- R&D spends stands at Rs 222.9 crs, 4% of revenue this quarter. In FY20, expects the R&D expenditure to be in the range of 4-4.5%, in FY21, the Co. expects it to be 6-6.5% as the biosimilars products will move to phase11 and Phase111.
- Net organic capex for the quarter US\$ 58 mn
- Net debt declined by US\$ 71 mn during the quarter taking total debt reduction of US\$ 202 mn in 1HFY20. In the next 3 years, the company expects to have zero debt for the existing business.
- EBITDA guidance – 57-58%

Exhibit: Sales and Sales Growth

Sales for the quarter grew by 18% YoY to Rs.5600 crs (vs our expectation of Rs.5596 crores)

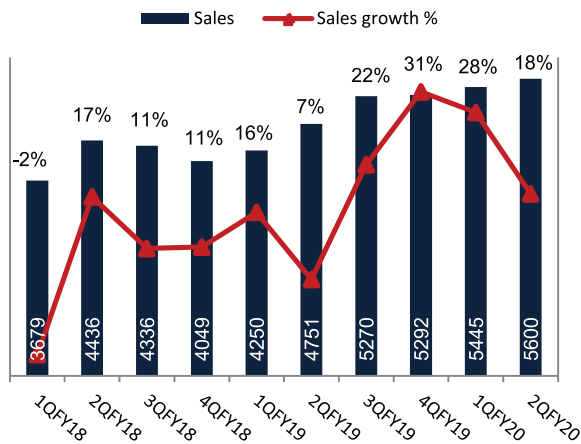


Exhibit: Gross and EBITDA margin

EBITDA margin shrank 75 bps YoY to 20.8% due to higher staff cost and other expenses.

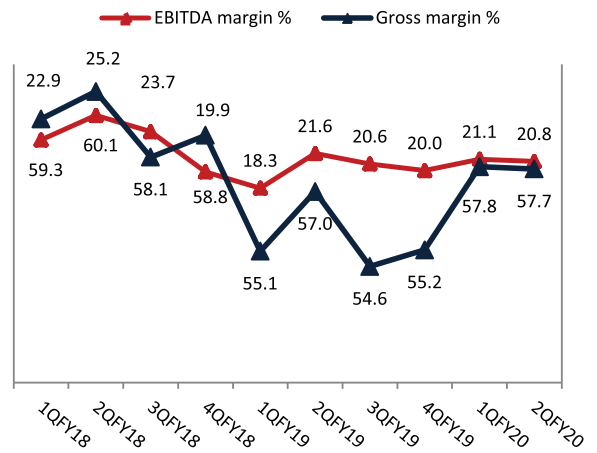


Exhibit: US sales and YoY growth

US sales grew by 27% YoY to US\$ 404 million on account of robust growth of the injectables business.

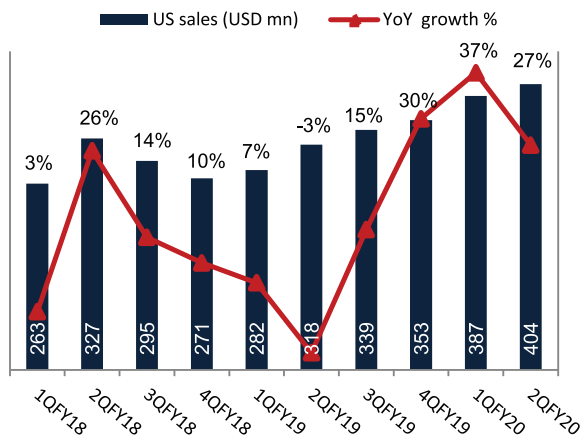


Exhibit: R&D cost and R&D as a % of sales

R&D spend is at Rs. 223 crs(4% of sales) this quarter v/s Rs. 217 crs in Q2FY20 (4.6% of sales).

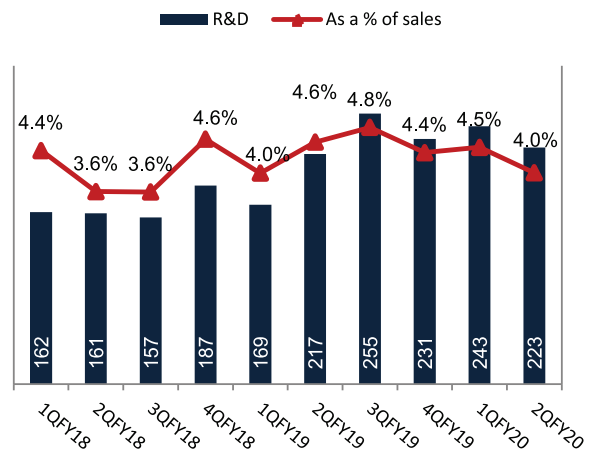
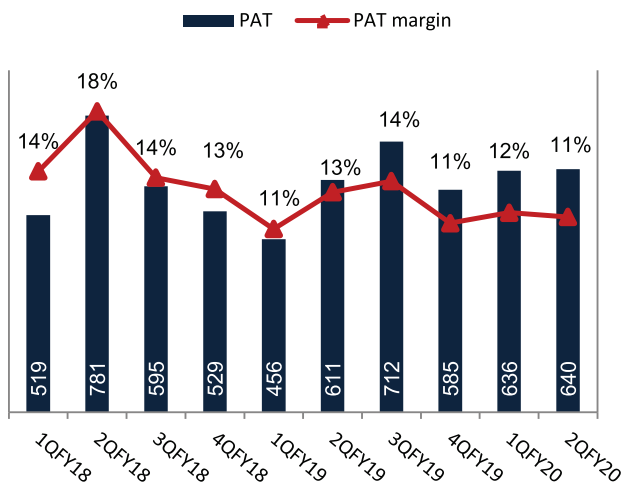


Exhibit: PAT and PAT margin

Adjusting for the forex loss of Rs.27.2 crs, the PAT grew by 9% YoY to Rs. 667 crs (vs our estimate of Rs. 698 crs).



Operational Details

Fig in Rs Cr

GEOGRAPHY	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
USA	2099	1910	1739	1890	2227	2433	2481	2688	2835
Europe	1114	1172	1152	1199	1157	1293	1312	1392	1401
Growth Markets	243	250	210	257	308	341	289	313	319
ARV	208	239	149	156	244	281	292	319	238
API	772	766	800	748	817	922	917	732	806

REVENUE GR. %	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
USA	21%	9%	6%	11%	6%	27%	43%	42%	27%
Europe	37%	37%	48%	31%	4%	10%	14%	16%	21%
Growth Markets	38%	33%	6%	32%	26%	36%	38%	22%	4%
ARV	-25%	-30%	-43%	-36%	18%	18%	96%	105%	-2%
API	0%	-1%	5%	20%	6%	20%	15%	-2%	-1%

REVENUE MIX%	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
USA	47%	44%	43%	44%	47%	46%	47%	49%	51%
Europe	25%	27%	28%	28%	24%	25%	25%	26%	25%
Growth Markets	5%	6%	5%	6%	6%	6%	5%	6%	6%
ARV	5%	6%	4%	4%	5%	5%	6%	6%	4%
API	17%	18%	20%	18%	17%	17%	17%	13%	14%

ANDA PIPELINE	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
ANDA filings	21	2	11	7	25	10	22	12	20
ANDA approvals	2	20	10	13	13	14	8	9	3

Financial Details

Balance Sheet

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	29	29	59	59	59	59	59	59
Reserves	3,721	5,127	7,229	9,313	11,622	13,832	16,390	19,113
Networth	3,750	5,156	7,287	9,372	11,680	13,891	16,449	19,172
Debt	3,634	3,864	4,415	3,084	4,483	6,753	5,713	5,713
Other Non Current Liab	215	235	47	88	291	339	412	421
Total Capital Employed	7,384	9,019	11,703	12,456	16,163	20,644	22,162	24,885
Net Fixed Assets (incl CWIP)	3,031	4,125	5,028	6,292	8,104	10,143	11,068	12,386
Non Current Investments	20	0	123	246	312	360	360	360
Other Non Current Assets	807	490	475	506	502	586	703	705
Non Current Assets	3,859	4,616	5,626	7,043	8,917	11,090	12,132	13,452
Inventory	2,368	3,611	4,056	4,331	5,858	7,246	8,053	8,673
Debtors	2,637	3,539	4,607	2,765	3,084	3,414	4,026	4,337
Cash & Bank	179	469	800	513	1,262	1,957	1,649	2,342
Other Current Assets	448	679	831	1,597	1,983	2,748	1,627	1,749
Current Assets	5,631	8,299	10,294	9,206	12,188	15,365	15,355	17,101
Creditors	1,351	2,051	2,457	2,155	2,627	2,677	3,097	3,336
Provisions	127	218	51	235	201	181	205	222
Other Current Liabilities	388	1,365	1,660	1,313	1,821	2,612	1,608	1,687
Curr Liabilities	1,865	3,634	4,168	3,703	4,649	5,470	4,911	5,245
Net Current Assets	3,766	4,664	6,127	5,503	7,539	9,895	10,444	11,856
Total Assets	9,490	12,914	15,920	16,249	21,105	26,454	27,487	30,553

Income Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	8,100	12,121	13,955	15,090	16,500	19,564	22,609	24,352
Change (%)	38%	50%	15%	8%	9%	19%	16%	8%
EBITDA	2132	2564	3188	3434	3772	3892	4745	4992
Change (%)	148%	20%	24%	8%	10%	3%	22%	5%
Margin (%)	26%	21%	23%	23%	23%	20%	21%	21%
Depr & Amor.	313	333	392	428	558	668	964	1065
EBIT	1819	2231	2796	3007	3214	3224	3781	3927
Int. & other fin. Cost	310	160	257	67	78	163	171	171
Other Income	23	97	204	116	102	116	80	122
EBT	1533	2168	2743	3056	3238	3177	3690	3878
Exp Item	-	-	-	-	-	88	25	-
Tax	363	597	721	760	818	727	949	992
Minority Int & P/L share of Ass.	4	5	3	5	3	3	5	-
Reported PAT	1,173	1,576	2,025	2,302	2,423	2,365	2,720	2,885
Adjusted PAT	1,173	1,576	2,025	2,302	2,423	2,297	2,701	2,885
Change (%)	299%	34%	29%	14%	5%	-2%	15%	6%
Margin(%)	14.5%	13.0%	14.5%	15.3%	14.7%	12.1%	12.0%	11.8%

Financial Details

Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	31%	31%	28%	25%	21%	17%	17%	15%
ROCE	36%	34%	35%	31%	26%	23%	23%	20%
Asset Turnover	0.85	0.94	0.88	0.93	0.78	0.74	0.82	0.80
Debtor Days	119	107	120	67	68	64	65	65
Inv Days	107	109	107	105	130	135	130	130
Payable Days	61	62	64	52	58	50	50	50
Int Coverage	6	14	11	45	41	20	22	23
P/E	12.7	11.3	21.5	17.2	13.5	19.5	9.2	8.6
Price / Book Value	4.0	3.5	6.0	4.2	2.8	3.3	1.5	1.3
EV/EBITDA	8	7	14	11	8	11	5	5
FCF per Share	9	16	(0)	27	7	3	18	18
Div Yield	0.0%	0.7%	0.3%	0.3%	0.7%	0.3%	0.6%	0.6%

Cash Flow Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	1,533	2,168	2,744	3,061	3,241	3,091	3,669	3,878
(inc)/Dec in Working Capital	(1,057)	(842)	(1,079)	583	(1,069)	(1,510)	(902)	(712)
Non Cash Op Exp	313	333	392	428	558	668	964	1,065
Int Paid (+)	94	71	79	55	63	151	171	171
Tax Paid	(344)	(496)	(733)	(774)	(752)	(770)	(949)	(992)
others	109	3	16	(73)	(86)	(8)	-	-
CF from Op. Activities	646	1,237	1,420	3,279	1,955	1,622	2,954	3,410
(inc)/Dec in FA & CWIP	(390)	(768)	(1,447)	(1,694)	(1,530)	(1,426)	(1,889)	(2,383)
Free Cashflow	256	469	(28)	1,584	425	196	1,065	1,027
(Pur)/Sale of Inv	(408)	45	(149)	(108)	(68)	(46)	-	-
others	(21)	(675)	152	15	(359)	26	-	-
CF from Inv. Activities	(819)	(1,398)	(1,445)	(1,787)	(1,957)	(2,877)	(1,889)	(2,383)
inc/(dec) in NW	3	7	7	7	0	0	-	-
inc/(dec) in Debt	267	341	603	(1,728)	1,202	2,230	(1,040)	-
Int. Paid	(94)	(74)	(84)	(57)	(74)	(152)	(171)	(171)
Div Paid (inc tax)	(60)	(180)	(162)	(137)	(264)	(160)	(162)	(162)
others								
CF from Fin. Activities	118	93	365	(1,915)	864	1,919	(1,373)	(333)
Inc(Dec) in Cash	(55)	(68)	340	(424)	862	664	(308)	693
Add: Opening Balance	203	529	404	743	350	1,211	1,957	1,649
Closing Balance	148	461	744	320	1,212	1,876	1,649	2,342

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Correspondence Office Address: Arch Waterfront, 5th Floor, Block GP, Saltlake, Sector 5, Kolkata 700 091; Tel No.: 033-40541700; www.narnolia.com.

Registered Office Address: Marble Arch, Office 201, 2nd Floor, 236B, AJC Bose Road, Kolkata 700 020; Tel No.: 033-4050 1500; www.narnolia.com

Compliance Officer: Manish Kr Agarwal, Email Id: mkagarwal@narnolia.com, Contact No.:033-40541700.

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