

# Sun Pharmaceutical Industries

3 August 2020

Reuters: SUN.NS; Bloomberg: SUNP IN

## Cost savings offset the impact of COVID lockdown

Sun Pharmaceutical Industries' (SPIL) 1QFY21 revenue at Rs75,853mn is down 7.3% QoQ and 9.4% YoY as there was a slowdown across geographies with India and API business being an exception. US sales (US\$282mn) declined by 33.5% YoY and 21% QoQ. Emerging Markets sales were down 10% YoY as the company lost tender sales in South Africa. Rest of the world sales declined by 18% YoY due to slowdown in Japan and lower sales of Taro Pharma (ex US). In line with the broader trend seen so far, API sales grew by 20% YoY and India sales were up in low single digits. Revenue is 5% above our estimate and 6% below consensus estimate. Despite weak revenue, EBITDA declined by just 7.6% YoY, growing by 35% QoQ, led by savings in operational costs. Despite a strong operational performance, the company reported a net loss of Rs16,556mn, owing to provisions of Rs31,781mn related to the settlement of an ongoing litigation with DoJ/State AG pertaining to collusion among generic players on price rigging of certain drugs. Adjusted for the same, the net profit stood at Rs11,460mn (adjusted EPS of Rs4.78).

The decline in US sales was due to slowdown in the sales of Taro Pharma and specialty pharma segment. Global sales of the specialty portfolio declined by US\$47mn QoQ from US\$125mn to US\$78mn in 1QFY21. Since majority of dermatologists were closed during the quarter, sales of medical benefit products like Ilumya and Levulan Kerastic witnessed a steep decline in usage. However, currently the prescriptions are back to pre COVID levels. Taro Pharma, which is also derma focused, saw a 27% decline in revenue. During the quarter, the company received an approval for the launch of Ilumya in Japan and it is preparing for its commercialization. The company is expected to leverage Pola Pharma's sales force for the launch of Ilumya in Japan.

EBITDA for the quarter (including other operating income) stood at Rs18,435mn, showing a growth of 35% QoQ and a decline of 7.6% YoY. The YoY number is not comparable due to a one-off business in the US in Q1FY20. The sequential growth in EBITDA is attributable to improvement in gross margin (up 219bps QoQ), led by a favorable business mix and decline in marketing, selling and travel expenses. This was partially offset by the higher employee costs arising from the hiring done in the US and India. These other expenses items will be lower in 2QFY21 but if the situation normalizes then we could see them return. The India branded generics business witnessed a growth of 3.2% YoY. The India branded generics business grew marginally as the Chronic segment showed a healthy growth of 10% YoY, but the business was affected by the 22% YoY negative growth in the Acute segment. We have maintained our estimates but revise our target valuation multiple to 23x (from 20x) to account for the litigation settlement that more or less addresses the overhang on the stock. Incrementally, the higher multiple is also to account for the investments made in globalization of its specialty portfolio. We retain our Buy rating with a new target price of Rs625 (from Rs543 earlier).

## BUY

**Sector:** Pharmaceuticals

**CMP:** Rs532

**Target Price:** Rs625

**Upside:** 18%

**Vishal Manchanda**

Research Analyst

vishal.manchanda@nirmalbang.com

+91-9737437148

**Gaurang Sakare**

Research Associate

gaurang.sakare@nirmalbang.com

+91-22 6273 8093

### Key Data

Current Shares O/S (mn)	2,399.3
Mkt Cap (Rsbn/US\$bn)	1,275.7/17.1
52 Wk H / L (Rs)	541/312
Daily Vol. (3M NSE Avg.)	10,769,530

### Price Performance (%)

	1 M	6 M	1 Yr
SPIL	12.4	22.4	24.6
Nifty Index	7.5	(7.4)	(0.4)

Source: Bloomberg

[Latest Annual Report](#)
[Latest MD&A](#)

Y/E March (Rsmn)	1QFY20	4QFY20	1QFY21	YoY (%)	QoQ (%)	FY19	FY20	YoY (%)
Revenues (Incl. Other Op. Revenues)	83,744	81,849	75,853	(9.4)	(7.3)	2,90,659	3,28,375	13.0
Raw material costs	24,578	23,048	19,696	(19.9)	(14.5)	78,690	92,305	17.3
%age of revenues	29.3	28.2	26.0	(338) bps	(219) bps	27.1	28.1	104 bps
Staff costs	15,404	16,519	17,590	14.2	6.5	59,671	63,624	6.6
%age of revenues	18.4	20.2	23.2	480 bps	301 bps	20.5	19.4	(115) bps
Other expenses	23,806	28,652	20,131	(15.4)	(29.7)	89,223	1,02,549	14.9
%age of revenues	28.4	35.0	26.5	(189) bps	(847) bps	30.7	31.2	53 bps
EBITDA	19,956	13,630	18,435	(7.6)	35.3	63,076	69,898	10.8
EBITDA margin (%)	23.8	16.7	24.3	47 bps	765 bps	21.7	21.3	(42) bps
Other income	2,130	1,022	1,538	(27.8)	50.4	10,255	6,360	(38.0)
Interest costs	1,041	518	520	(50.1)	0.3	5,553	3,027	(45.5)
Depreciation	4,571	5,754	4,959	8.5	(13.8)	17,533	20,528	17.1
Exceptional item	0	-2,606	-36,333	-	-	-12,144	-2,606	-
PBT	16,474	5,774	-21,839	-	-	38,102	50,096	31.5
Tax	1,461	831	2,459	68.4	196.0	6,249	8,228	31.7
Tax rate (%)	8.9	14.4	(11.3)	-	-	16.4	16.4	2 bps
PAT before MI	15,014	4,944	-24,298	-	-	31,853	41,868	31.4
MI and shares of associates	-1,139	-945	7,742	-	-	-5,439	-4,219	(22.4)
PAT	13,875	3,998	-16,556	-	-	26,414	37,649	42.5
PAT margin (%)	16.6	4.9	(21.8)	-	-	9.1	11.5	238 bps

Source: Company, Nirmal Bang Institutional Equities Research

## Concall Highlights

**Impact of Covid-19:** The company is conducting the trials on two drugs to repurpose them for Covid-19 and will be announcing results after two quarters. Due to the various compliance procedures involved in different countries, these drugs will for now be limited to India.

**Specialty business:** The specialty business at US\$78mn declined QoQ. Ilumya and Levulan were affected as they are clinically administered. Levulan was especially affected as it is only given in clinics. However, the company has reported that there is no loss in market share. Some of the products will start to achieve breakeven from the next financial year.

**Ilumya:** The company has received an approval for the launch of Ilumya in Japan and is preparation of its launch. The company has also partnered with Hikma for marketing the product in the Middle East and North Africa.

**Absorica:** The shift from Absorica to Absorica LD is taking longer than usual due to the Covid-19 pandemic.

**India business:** The India business was down due to closure of clinics. The OPDs are gradually opening up and the field force has started doctor visits again. There were no physical visits to doctors in April and half of May. The expansion of field force in India is nearing completion. The company launched 10 new products in India digitally.

**R&D:** The R&D spend for 1QFY21 stood at Rs4,152mn, which is 5.6% of sales. The company spent 39% of the R&D expenditure on specialty products.

**Debt:** The company reduced its debt by US\$200mn in 1QFY21 and the net debt stood at US\$451mn, excluding Taro.

**Halol plant:** The company has almost completed the remediation work and is awaiting for USFDA's response.

**Tax rate:** The tax rate should inch up from FY20 levels.

**API business incentive from GOI:** The company is evaluating certain APIs where it would intend to invest and avail benefits of the bulk drug policy laid out by the government.

### Exhibit 1: Key financials

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Net sales	2,64,895	2,90,659	3,28,375	3,60,664	3,85,108
EBITDA	56,081	63,076	69,898	91,522	1,00,755
Net profit	21,616	26,654	37,649	58,813	65,196
EPS (Rs)	9.0	11.1	15.7	24.5	27.2
EPS growth (%)	(69.0)	23.3	41.3	56.2	10.9
EBITDA margin (%)	21.2	21.7	21.3	25.4	26.2
PER (x)	48.3	39.2	27.7	17.7	16.0
P/BV (x)	2.7	2.5	2.3	2.1	1.9
EV/EBITDA (x)	18.1	16.5	14.9	11.1	9.4
RoCE (%)	12.0	12.7	9.6	13.2	13.4
RoE (%)	13.6	14.2	14.0	16.4	16.3

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 2: Actual performance versus our estimate and Bloomberg consensus estimate

(Rsmn)	Actual	NBIE est.	Var.(%)	Consensus est.	Var.(%)
Revenues	75,853	72,133	5.2	80,636	(5.9)
EBITDA	18,435	12,560	46.8	16,871	9.3
EBITDA margin (%)	24.3	17.4	689 bps	20.9	340 bps
PAT	-16,556	5,849	-	9,546	-
PAT margin (%)	-21.8	8.1	-	11.8	-

Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 3: Revenue Summary**

Revenue summary	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21
India Branded Generics	21,520	18,597	22,353	11,013	23,137	25,148	25,170	23,648	23,884
US Formulations	25,437	23,979	26,059	31,238	29,474	23,898	24,924	27,129	21,364
Emerging Markets	13,087	13,720	14,618	12,199	13,486	14,117	13,901	13,540	13,161
Western Europe & Other Markets	7,178	7,615	8,981	10,780	11,591	11,371	11,035	11,212	10,300
<b>Sub-Total</b>	<b>67,222</b>	<b>63,911</b>	<b>72,010</b>	<b>65,231</b>	<b>77,688</b>	<b>74,533</b>	<b>75,031</b>	<b>75,529</b>	<b>68,709</b>
Bulk Drugs & Others	4,167	4,554	4,557	5,211	4,905	4,959	5,356	5,252	5,963
<b>Total</b>	<b>71,389</b>	<b>68,465</b>	<b>76,567</b>	<b>70,443</b>	<b>82,593</b>	<b>79,492</b>	<b>80,387</b>	<b>80,780</b>	<b>74,672</b>
Revenue Mix	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21
India Branded Generics	30.1	27.2	29.2	15.6	28.0	31.6	31.3	29.3	32.0
US Formulations	35.6	35.0	34.0	44.3	35.7	30.1	31.0	33.6	28.6
Emerging Markets	18.3	20.0	19.1	17.3	16.3	17.8	17.3	16.8	17.6
Western Europe & Other Markets	10.1	11.1	11.7	15.3	14.0	14.3	13.7	13.9	13.8
Bulk Drugs & Others	5.8	6.7	6.0	7.4	5.9	6.2	6.7	6.5	8.0
Y-O-Y Growth (%)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21
India Branded Generics	22.2	(16.3)	7.2	(43.9)	7.5	35.2	12.6	114.7	3.2
US Formulations	12.3	20.7	22.7	31.7	15.9	(0.3)	(4.4)	(13.2)	(27.5)
Emerging Markets	21.1	9.0	19.7	(4.6)	3.0	2.9	(4.9)	11.0	(2.4)
Western Europe & Other Markets	(3.3)	7.1	15.6	45.0	61.5	49.3	22.9	4.0	(11.1)
Bulk Drugs & Others	34.9	17.3	23.2	56.8	24.4	16.3	25.7	8.6	29.3
Total	15.8	3.9	16.0	5.0	15.7	16.1	5.0	14.7	(9.6)
Q-O-Q Growth (%)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21
India Branded Generics	9.7	(13.6)	20.2	(50.7)	110.1	8.7	0.1	(6.0)	1.0
US Formulations	7.3	(5.7)	8.7	19.9	(5.6)	(18.9)	4.3	8.8	(21.2)
Emerging Markets	2.3	4.8	6.5	(16.5)	10.5	4.7	(1.5)	(2.6)	(2.8)
Western Europe & Other Markets	(3.5)	6.1	17.9	20.0	7.5	(1.9)	(3.0)	1.6	(8.1)
Bulk Drugs & Others	17.8	9.3	0.1	14.4	(5.9)	1.1	8.0	(1.9)	13.6
Total	6.4	(4.1)	11.8	(8.0)	17.2	(3.8)	1.1	0.5	(7.6)

Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 4: Margin Summary**

Margins (%)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21
Gross Margin	70.8	74.7	72.0	74.3	70.7	72.1	73.0	71.8	74.0
EBITDA Margin	22.2	22.1	27.8	14.2	23.8	22.0	22.6	16.7	24.3
EBIT Margin	16.7	15.9	21.7	7.9	18.4	16.2	15.9	9.6	17.8
PAT Margin	13.6	(3.2)	16.0	8.9	16.6	13.1	11.2	4.9	(21.8)

Source: Company, Nirmal Bang Institutional Equities Research

## Financial statement

### Exhibit 5: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
<b>Net sales</b>	<b>2,64,895</b>	<b>2,90,659</b>	<b>3,28,375</b>	<b>3,60,664</b>	<b>3,85,108</b>
Growth (%)	(16.1)	9.7	13.0	9.8	6.8
Raw material costs	74,247	78,690	92,305	95,837	1,04,133
Employee expenses	53,671	59,671	63,624	68,764	74,609
Other expenses	80,896	89,223	1,02,549	1,04,541	1,05,611
Total expenditure	2,08,813	2,27,583	2,58,477	2,69,142	2,84,353
<b>EBITDA</b>	<b>56,081</b>	<b>63,076</b>	<b>69,898</b>	<b>91,522</b>	<b>1,00,755</b>
Growth (%)	(44.4)	12.5	10.8	30.9	10.1
EBITDA margin (%)	21.2	21.7	21.3	25.4	26.2
Other income	8,388	10,255	6,360	12,408	13,649
Interest costs	5,176	5,553	3,027	4,528	3,940
Gross profit	1,90,648	2,11,969	2,36,071	2,64,827	2,80,975
% growth	(18.7)	11.2	11.4	12.2	6.1
Depreciation	14,998	17,533	20,528	19,461	21,216
Exceptional items	-9,505	-12,144	-2,606	0	0
<b>PBT</b>	<b>34,790</b>	<b>38,102</b>	<b>50,096</b>	<b>79,941</b>	<b>89,248</b>
% growth	(61.5)	9.5	31.5	59.6	11.6
Tax	8,452	6,009	8,228	15,988	19,188
Effective tax rate (%)	24.3	15.8	16.4	20.0	21.5
<b>PAT before MI</b>	<b>26,084</b>	<b>32,079</b>	<b>41,720</b>	<b>63,953</b>	<b>70,059</b>
MI	4,468	5,424	4,070	5,140	4,864
<b>PAT</b>	<b>21,616</b>	<b>26,654</b>	<b>37,649</b>	<b>58,813</b>	<b>65,196</b>
Growth (%)	(66.8)	23.0	30.1	53.3	9.5
<b>EPS (Rs)</b>	<b>9.0</b>	<b>11.1</b>	<b>15.7</b>	<b>24.5</b>	<b>27.2</b>
EPS growth (%)	(69.0)	23.3	41.3	56.2	10.9

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 7: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
Equity	2,399	2,399	2,399	2,399	2,399
Reserves	3,78,606	4,11,691	4,50,245	4,99,461	5,55,059
Net worth	3,81,006	4,14,091	4,52,645	5,01,860	5,57,458
Minority interest	38,842	33,135	38,602	43,743	48,606
Total Loans	1,11,212	1,09,238	88,655	94,954	85,613
Deferred tax liabilities	3,518	2,312	2,602	2,602	2,602
Other non-current liabilities	4,311	10,016	12,919	12,919	12,919
<b>Total liabilities</b>	<b>5,38,887</b>	<b>5,68,792</b>	<b>5,95,423</b>	<b>6,56,077</b>	<b>7,07,198</b>
Fixed assets including CWIP	1,05,935	1,09,382	1,12,263	1,13,575	1,18,705
Goodwill & intangible assets	1,07,243	1,23,095	1,28,409	1,17,788	1,17,942
Long-term loans & advances	23,474	958	1,057	1,057	1,057
Other non-current assets	90,017	1,02,811	1,24,254	1,29,254	1,34,254
Inventories	68,807	78,860	78,750	85,334	92,721
Debtors	78,153	88,842	94,212	98,812	1,05,509
Cash and cash equivalents	79,254	70,623	56,766	1,12,629	1,50,594
Bank balances other than cash	20,040	2,133	8,109	35,000	35,000
Other current assets	70,106	70,234	78,704	75,704	72,704
<b>Total current assets</b>	<b>3,16,359</b>	<b>3,10,692</b>	<b>3,16,542</b>	<b>4,07,479</b>	<b>4,56,528</b>
Creditors	47,662	41,479	40,937	52,513	57,059
Other current liabilities/provisions	56,479	36,667	46,165	60,562	64,229
<b>Total current liabilities</b>	<b>1,04,141</b>	<b>78,146</b>	<b>87,102</b>	<b>1,13,076</b>	<b>1,21,288</b>
Net current assets	2,12,218	2,32,546	2,29,440	2,94,403	3,35,240
Assets held for sale	0	0	0	0	0
<b>Total assets</b>	<b>5,38,887</b>	<b>5,68,792</b>	<b>5,95,423</b>	<b>6,56,077</b>	<b>7,07,198</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 6: Cash flow

Y/E March (Rsmn)	FY18	FY19	FY20	FY21E	FY22E
PBT	44,295	50,246	52,702	79,941	89,248
(Inc.)/dec. in working capital	6,601	-26,802	-878	392	-9,538
<b>Cash flow from operations</b>	<b>50,896</b>	<b>23,444</b>	<b>51,825</b>	<b>80,333</b>	<b>79,709</b>
Other income	-8,388	-10,255	-6,360	-12,408	-13,649
Interest paid	5,176	5,553	3,027	4,528	3,940
Depreciation	14,998	17,533	20,528	19,461	21,216
DTL&DTA	1,243	-5,581	-7,096	0	0
Tax paid (-)	8,452	6,009	8,228	15,988	19,188
<b>Net cash from operations</b>	<b>55,473</b>	<b>24,684</b>	<b>53,696</b>	<b>75,926</b>	<b>72,029</b>
Capital expenditure (-)	-23,411	-36,831	-28,723	-10,152	-26,500
<b>Net cash after Capex</b>	<b>32,062</b>	<b>-12,147</b>	<b>24,972</b>	<b>65,774</b>	<b>45,529</b>
Other investing activities	-71,581	25,489	-17,001	10,408	11,649
Cash from financial activities	-12,596	-39,880	-15,852	6,571	-19,212
Change in cash balance	-52,115	-26,538	-7,881	82,753	37,966
Opening cash balance	1,51,408	99,294	72,756	64,876	1,47,629
Closing cash balance	99,294	72,756	64,875	1,47,629	1,85,594

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 8: Key ratios

Y/E March	FY18	FY19	FY20	FY21E	FY22E
<b>Profitability &amp; return ratios</b>					
EBITDA margin (%)	21.2	21.7	21.3	25.4	26.2
EBIT margin (%)	18.7	19.2	17.0	23.4	24.2
Net profit margin (%)	9.9	11.0	12.8	17.7	18.2
RoE (%)	13.6	14.2	14.0	16.4	16.3
RoCE (%)	12.0	12.7	9.6	13.2	13.4
<b>Working capital &amp; liquidity ratios</b>					
Receivables (days)	28	29	28	27	27
Inventory (days)	120	118	111	115	118
Payables (days)	80	71	58	65	73
Working capital (days)	68	76	81	76	72
Current ratio (x)	1.6	1.8	2.0	2.1	2.4
Cash ratio (x)	0.7	0.6	0.7	1.0	1.2
<b>Valuation ratios</b>					
EV/Sales (x)	3.8	3.6	3.2	2.8	2.5
EV/EBITDA (x)	18.1	16.5	14.9	11.1	9.4
P/E (x)	48.3	39.2	27.7	17.7	16.0
P/BV (x)	2.7	2.5	2.3	2.1	1.9

Source: Company, Nirmal Bang Institutional Equities Research

## P/E Chart

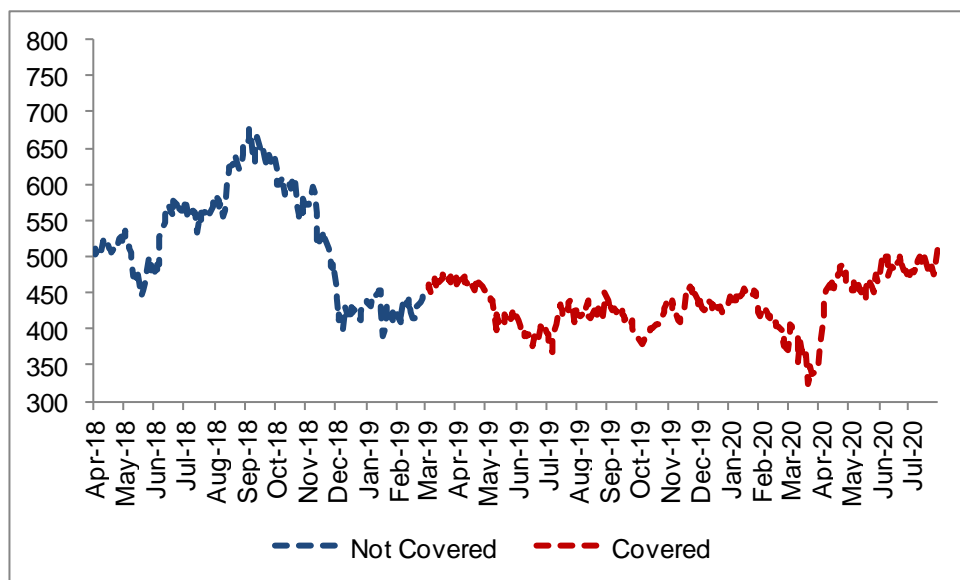


Source: BSE, Bloomberg, Nirmal Bang Institutional Equities Research

## Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
5 March 2019	Buy	446	581
5 April 2019	Buy	462	581
29 May 2019	Buy	414	578
14 August 2019	Buy	438	578
23 September 2019	Buy	414	573
8 November 2019	Buy	440	517
7 February 2020	Buy	431	517
27 March 2020	Buy	339	489
23 April 2020	Buy	474	543
27 May 2020	Buy	451	543
3 August 2020	Buy	532	625

## Rating track graph



**DISCLOSURES**

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### Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

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Team Details:			
Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	-
Girish Pai	Head of Research	girish.pai@nirmalbang.com	+91 22 6273 8017 / 18
Dealing			
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 6273 8230, +91 22 6636 8833
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 6273 8102/8103, +91 22 6636 8830

## Nirmal Bang Equities Pvt. Ltd.

### Correspondence Address

B-2, 301/302, Marathon Innova,  
 Nr. Peninsula Corporate Park,  
 Lower Parel (W), Mumbai-400013.

Board No. : 91 22 6273 8000/1; Fax. : 022 6273 8010