

Sun Pharma

Performance Highlights

(₹ cr)	2QFY2017	1QFY2017	% chg (qoq)	2QFY2016	% chg (yoy)
Net sales	7,764	8,007	(3.0)	6,858	13.2
Other income	621	393	57.7	130	376.0
Gross profit	5,924	6,160	(3.8)	5,360	10.5
Operating profit	2,667	2,685	(0.7)	1,858	43.5
Adj. Net profit	2,235	2,034	9.9	1,029	117.3

Source: Company, Angel Research

Sun Pharma posted numbers better than expected on OPM and net profit front. Sales came in at ₹7,764cr vs. ₹7,800cr expected vs. ₹6,858cr in 2QFY2016, posting a yoy growth of 13.2%. On the operating front, the EBITDA margin came in at 34.3% vs. 30.1% expected and vs. 27.1% in 2QFY2016. Lower expenses during the quarter aided the OPM expansion. Consequently, the Adj. PAT came in at ₹2,235cr vs. ₹1,545cr expected vs. ₹1,029cr in 2QFY2016, a yoy growth of 117.3%. Apart from better than expected OPM, the company also posted higher than expected other income (₹621cr in 2QFY2017 vs. ₹226cr in 2QFY2016). **We maintain our Buy rating on the stock.**

Results mostly better than expectations: Sun Pharma posted sales of ₹7,764cr vs. ₹7,800cr expected vs. ₹6,858cr in 2QFY2016, posting a yoy growth of 13.2%. India sales at ₹2,009cr, was up by 11% yoy. US finished dosage sales at US\$555mn, was up by 9% yoy. Emerging markets sales stood at US\$170mn, up by 22% yoy. Rest of World (ROW) sales stood at US\$ 79mn, growth of 3% yoy. On the operating front, the EBITDA margin came in at 34.3% vs. 30.1% expected and vs. 27.1% in 2QFY2016. Consequently, the Adj. PAT came in at ₹2,235cr vs. ₹1,545cr expected vs. ₹1,029cr in 2QFY2016, a yoy growth of 117.3%. Apart from better than expected OPM, the company also posted higher than expected other income (₹621cr in 2QFY2017 vs. ₹226cr in 2QFY2016).

Outlook and valuation: Sun Pharma is one of the largest and fastest growing Indian pharmaceutical companies. We expect its net sales to post a CAGR of 12.7% (including Ranbaxy Laboratories) to ₹35,258cr and EPS to post a CAGR of 26.5% to ₹35.3 over FY2016–18E. **We recommend a Buy rating on the stock.**

Key financials (Consolidated)

Y/E March (₹ cr)	FY2015	FY2016	FY2017E	FY2018E
Net sales	27,287	27,744	31,129	35,258
% chg	70.6	1.7	12.2	13.3
Adj. Net profit	4,743	5,306	7,260	8,495
% chg	(10.0)	11.9	36.8	17.0
EPS (₹)	22.9	22.0	30.2	35.3
EBITDA margin (%)	28.6	26.2	32.0	32.9
P/E (x)	29.8	31.0	22.6	19.4
RoE (%)	21.1	18.3	20.0	20.1
RoCE (%)	21.1	16.6	19.0	19.1
P/BV (x)	6.2	4.5	3.7	3.0
EV/Sales (x)	5.1	5.8	4.9	4.2
EV/EBITDA (x)	17.7	22.0	15.4	12.6

Source: Company, Angel Research; Note: CMP as of November 15, 2016

BUY

CMP	₹683
Target Price	₹847

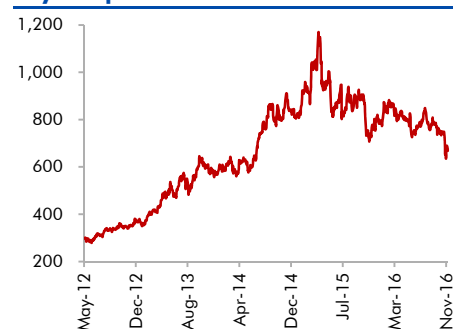
Investment Period	12 months
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Stock Info	
Sector	Pharmaceutical
Market Cap (₹ cr)	164,261
Net Debt (₹ cr)	(6,960)
Beta	0.7
52 Week High / Low	898/572
Avg. Daily Volume	431,125
Face Value (₹)	1
BSE Sensex	26,305
Nifty	8,108
Reuters Code	SUN.BO
Bloomberg Code	SUNP@IN

Shareholding Pattern (%)	
Promoters	55.0
MF / Banks / Indian Fls	12.9
FII / NRIs / OCBs	25.1
Indian Public / Others	7.0

Abs. (%)	3m	1yr	3yr
Sensex	(6.6)	2.7	28.9
Sun Pharma	(14.9)	(8.0)	13.8

3-year price chart



Source: Company, Angel Research

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Exhibit 1: 2QFY2017 performance (Consolidated)

Y/E March (₹ cr)	2QFY2017	1QFY2017	% chg QoQ	2QFY2016	% chg yoy	1HFY2017	1HFY2016	% chg
Net sales	7,764	8,007	(3.0)	6,858	13.2	15,771	13,329	18.3
Other income	620.5	393.4	57.7	130.4	376.0	1,014	566.4	79.0
Total income	8,385	8,400	(0.2)	6,989	20.0	16,785	13,895	20.8
Gross profit	5,924	6,160	(3.8)	5,360	10.5	12,084	10,050	20.2
Gross margin (%)	76.3	76.9		78.2		76.6	75.4	
Operating profit	2,667	2,685	(0.7)	1,858	43.5	5,352	3,514	52.3
Operating margin (%)	34.3	33.5		27.1		33.9	26.4	
Interest	54	135	(60.1)	158	(66.0)	188	271	(30.5)
Depreciation	304	316	(3.8)	258	17.6	620	511	21.3
Extraordinary item loss/ (gain)	0	0		0		0	685	
PBT	2,930	2,628	11.5	1,572	86.4	5,557	3,298	68.5
Provision for taxation	441.7	352.7	25.2	294.6	31.6	794	562	41.3
PAT before extra-ordinary item	2,488	2,275	9.4	1,277	78.8	4,763	2,736	74.1
Minority interest(MI)	253	241	4.8	248	1.9	446	464	(3.9)
Reported PAT	2,235	2,034	9.9	1,029	117.3	4,269	2,272	87.9
Adj. PAT	2,235	2,034	9.9	1,029	117.3	4,269	1,586	169.2
Adj. EPS (₹)	9.3	8.4		4.3		17.7	9.4	

Source: Company, Angel Research

Exhibit 2: 2QFY2017 – Actual V/s Angel estimates

(₹ cr)	Actual	Estimates	Variance (%)
Net sales	7,764	7,800	(0.5)
Other income	621	226	175.0
Operating profit	2,667	2,350	13.5
Tax	442	353	25.2
Adj. Net profit	2,235	1,545	44.7

Source: Company, Angel Research

Numbers just in line with expectations: Sun Pharma posted numbers better than expected on OPM and net profit front. Sales came in at ₹7,764cr vs. ₹7,800cr expected vs. ₹6,858cr in 2QFY2016, posting a yoy growth of 13.2%. India sales at ₹2,009cr, was up by 11% yoy. US finished dosage sales at US\$555mn, was up by 9% yoy. Emerging markets sales stood at US\$170mn, up by 22% yoy. Rest of World (ROW) sales stood at US\$ 79mn, growth of 3% yoy.

Amongst the key markets- India (₹2,009cr) posted a growth of 11.0% yoy, US (US\$555mn) posted a growth of 9.0% yoy, Emerging markets (US\$170mn) were up by 22% yoy and ROW (US\$79mn) a growth of 3.0% yoy.

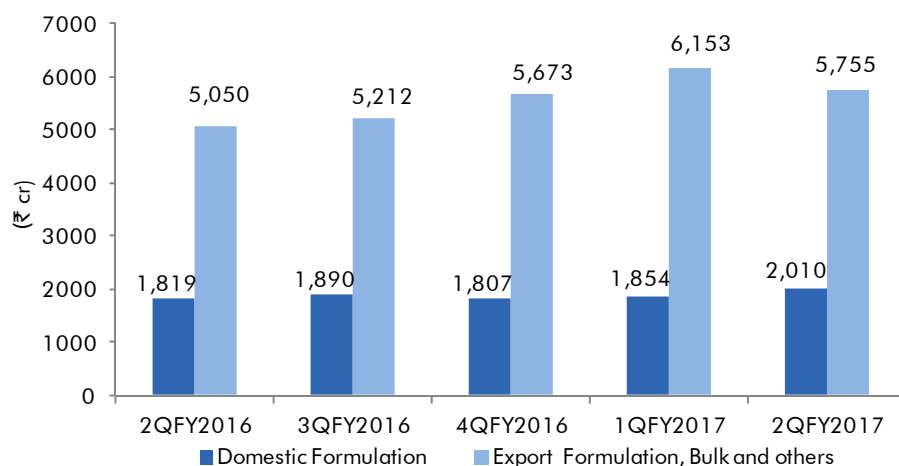
Sale of branded formulations in India for 2QFY2017 stood at ₹2,009cr, up by 11.0% yoy and accounted for 26% of total sales. Sun Pharma is ranked No. 1 and holds ~8.7% market share in the Rs. 100,000cr pharmaceutical market as per the September-2016 AIOCD-AWACS report.

Sales in the US came in at US\$555mn for the quarter, accounting for 48% of total sales. Sales in emerging markets were at US\$170mn for 2QFY2017, a yoy growth of 22% and accounted for 15% of total sales. Formulation sales in Rest of World (ROW) markets excluding US and Emerging markets were US\$79mn in

2QFY2017, a growth of 22.0% yoy and accounted for ~7% of revenues for the quarter.

The company had a total of 423 ANDAs filed with the USFDA. Currently, ANDAs for 144 products await USFDA approval, including 13 tentative approvals.

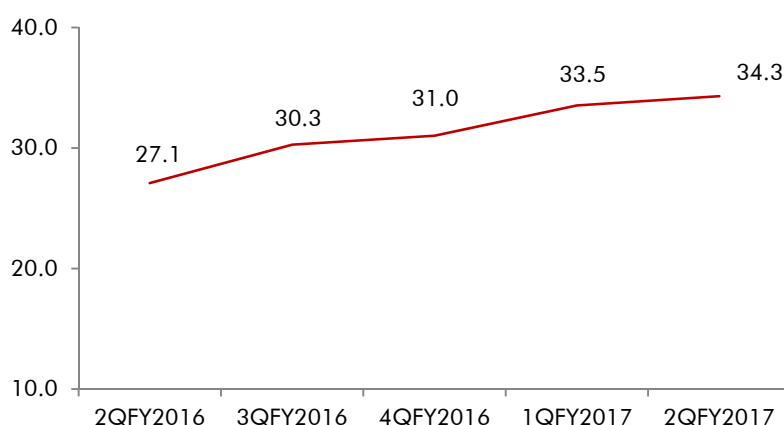
Exhibit 3: Sales trend



Source: Company, Angel Research

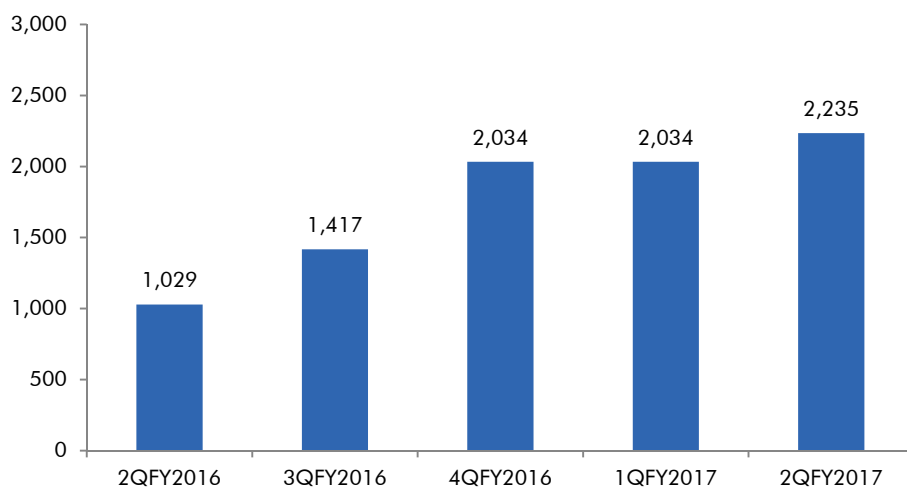
OPM at 34.3%; higher than an expected 30.1%: On the operating front, the EBITDA margin came in at 34.3% vs. 30.1% expected and vs. 27.1% in 2QFY2016. Lower expenses during the quarter aided the OPM expansion. Employee and other expenses, during the quarter, posted a decline of 2.0% and 8.0%, respectively. The R&D expenses came in at 7.3% of sales, same in line with last year, posting a yoy growth of 14.0%.

Exhibit 4: OPM trend (%)



Source: Company, Angel Research,

Net profit came in higher than our expectation: Consequently, the Adj. PAT came in at ₹2,235cr vs. ₹1,545cr expected vs. ₹1,029cr in 2QFY2016, a yoy growth of 117.7%. Apart from better than expected OPM, the company also posted higher than expected other income (₹621cr in 2QFY2017 vs. ₹226cr in 2QFY2016).

Exhibit 5: Adjusted Net profit trend (₹ cr)


Source: Company, Angel Research

Concall takeaways

- Management guided that the company has completed the remediation process and has re-invited the USFDA for a re-inspection, though the timing of the re-inspection and potential clearance thereafter remains unpredictable.
- Ranbaxy integration is progressing ahead of management's expected timelines, and management expects the acquisition to deliver synergies of US\$300mn by FY2018. The focus areas for integration include cGMP compliance, sourcing efficiencies as well as revenue synergies.
- NLEM impact to be ~₹1,500cr in FY2017.
- Management also guided on pressures in the domestic market on account of WPI-led price cuts on NLEM portfolio, though it expects growth to revive in the coming quarters.
- R&D expenses to be 9% in FY2017.

Investment arguments

Strongest ANDA pipeline: Sun Pharma, with the recent acquisitions of DUSA, URL Pharma and Ranbaxy Laboratories, has now become strong in the US region, with the geography accounting for 52% of its sales in FY2016. In terms of ANDAs, the company cumulatively has 423 products, out of which 144 products now await USFDA approval, including 13 tentative approvals. With the merger of Ranbaxy Laboratories, the company is now the fifth-largest specialty generics company in the world (behind Teva, Sandoz, Actavis and Mylan). However, the near term performance of the company has been impacted on back of supply constraints at the Halol facility, although the company has taken redemption measures including site transfers. Overall, we expect the region to post a CAGR of 14.5% in sales over FY2016-18E, accounting for almost 49% of the overall sales in FY2018E.

Domestic business: Sun Pharma's domestic formulation business is among the fastest growing in the Indian pharmaceutical industry. It contributed 23% to the company's total turnover in FY2014. Sun Pharma, with Ranbaxy Laboratories'

merger, is now the segment leader with a market share of 8.7% in the domestic formulation market, followed by Abbott India which has a market share of 6.5%. This is a significant gap considering that the segment is highly fragmented. We expect the domestic formulation business to post a CAGR of 12.5% over FY2016-18E, contributing 25% to the overall formulation sales of the company in FY2018.

Healthy balance sheet: Sun Pharma has one of the strongest balance sheets in the sector with cash of ~₹15,000cr. The same can continue to support the Management in inorganic growth and in scouting for acquisitions, especially in the US and in emerging markets.

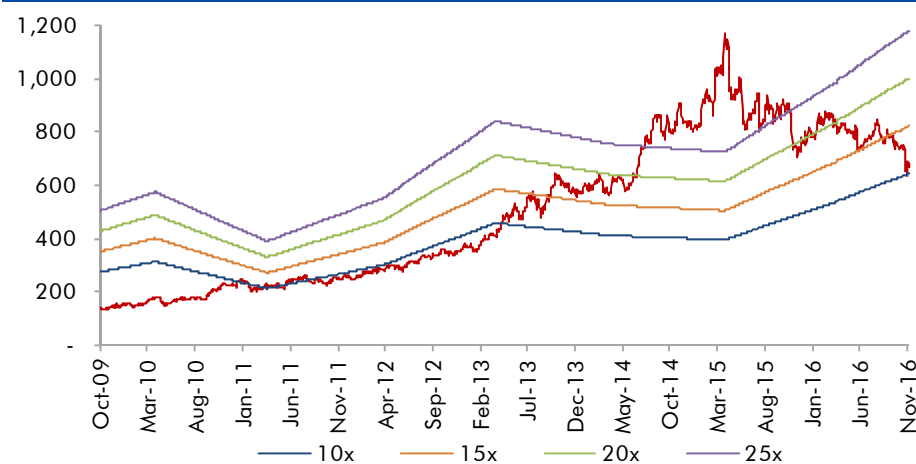
Outlook and valuation: Sun Pharma is one of the largest and fastest growing Indian pharmaceutical companies. We expect its net sales to post a CAGR of 12.7% (including Ranbaxy Laboratories) to ₹35,258cr and EPS to post a CAGR of 26.5% to ₹35.3 over FY2016-18E. **We recommend a Buy rating on the stock.**

Exhibit 6: Key assumptions

	FY2017E	FY2018E
Domestic Formulation sales growth (%)	10.0	15.0
Export Formulation sales growth (%)	14.3	13.5
Growth in employee expenses (%)	15.0	20.0
Operating margins (%)	32.0	32.9
Tax as % of PBT	15.0	14.0

Source: Company, Angel Research

Exhibit 7: One-year forward PE band



Source: Company, Angel Research

Exhibit 8: Valuation summary

Company	Reco	CMP	Tgt. price	Upside	FY2018E			FY16-18E	FY2018E	
		(₹)	(₹)	%	PE (x)	EV/Sales (x)	EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma	Neutral	631	-	-	20.7	2.8	13.0	(10.8)	27.5	25.3
Aurobindo Pharma	Buy	733	877	19.7	15.5	2.7	11.5	18.1	22.5	26.1
Cadila Healthcare	Accumulate	358	400	11.7	18.7	2.9	13.0	13.4	22.7	25.7
Cipla	Neutral	553	-	-	20.3	2.6	14.0	20.4	13.5	15.2
Dr Reddy's	Neutral	3,309	-	-	22.9	2.9	13.3	1.7	16.2	15.9
Dishman Pharma	Neutral	229	-	-	20.2	3.0	10.0	3.1	10.3	10.9
GSK Pharma*	Neutral	2,650	-	-	43.6	6.6	32.0	17.3	35.3	32.1
Indoco Remedies	Sell	286	240	(18.5)	17.9	2.1	11.5	33.2	19.1	20.1
Ipca labs	Accumulate	540	613	13.4	27.5	1.9	12.4	36.5	8.8	9.4
Lupin	Buy	1,440	1,809	25.6	20.8	3.4	12.8	17.2	24.4	20.9
Sanofi India*	Neutral	4,253	-	-	24.7	2.6	17.7	22.2	24.9	28.8
Sun Pharma	Buy	683	847	24.0	19.4	4.2	12.6	26.5	19.1	20.1

Source: Company, Angel Research; Note: * December year ending

Company background

Sun Pharma is an international specialty pharma company, with a large presence in the US and India, and a footprint across 40 other markets. In India and rest of the world markets, the key chronic therapy areas for the company are cardiology, psychiatry, neurology, gastroenterology, diabetology etc. The company is a market leader in specialty therapy areas in India. In India, the company has emerged as a leading pharma company, where it is the third largest player. Also, in the US, a key geography, the company has expanded significantly through both in-organic and organic routes.

Profit & Loss statement (Consolidated)

Y/E March (₹ cr)	FY2014	FY2015	FY2016	FY2017E	FY2018E
Gross sales	16,200	27,652	28,110	31,412	35,578
Less: Excise duty	195	366	366	283	320
Net sales	16,004	27,287	27,744	31,129	35,258
Other operating income	76	147	526	526	526
Total operating income	16,080	27,433	28,270	31,655	35,784
% chg	42.3	70.6	3.0	12.0	13.0
Total expenditure	9,081	19,470	20,473	21,177	23,643
Net raw materials	2,779	6,739	6,483	7,274	8,239
Other mfg costs	699	1,192	1,212	1,360	1,540
Personnel	2,074	4,430	4,797	5,382	6,459
Other	3,528	7,109	7,981	7,160	7,404
EBITDA	6,923	7,817	7,271	9,953	11,615
% chg	41.1	12.9	-7.0	-18.0	-14.1
(% of Net Sales)	43.3	28.6	26.2	32.0	32.9
Depreciation & amort.	409	1,195	1,014	1,214	1,414
EBIT	6,514	6,622	6,783	9,265	10,727
% chg	42.5	1.7	2.4	(15.0)	15.8
(% of Net Sales)	40.7	24.3	24.4	29.8	30.4
Interest & other charges	44	579	477	477	477
Other income	552	451	1,050	1,050	1,050
(% of PBT)	7.8	6.8	14.3	10.7	9.3
Share in profit of Asso.	-	-	-	-	-
Recurring PBT	7,098	6,641	7,356	9,838	11,300
% chg	44.9	-6.4	10.8	(9.9)	0.0
Extraordinary expense/(inc.)	2,517	237.8	590.5	-	-
PBT (reported)	7,098	6,641	6,765	9,848	11,300
Tax	702.2	914.7	934.9	1,477.2	1,695.0
(% of PBT)	9.9	13.8	13.8	15.0	15.0
PAT (reported)	6,396	5,726	5,830	8,371	9,605
Add: Share of earnings of asso.	-	(13)	(2)	-	-
Less: Minority interest (MI)	738	936	1,111	1,111	1,111
Prior period items	-	-	-	-	-
PAT after MI (reported)	3,141	4,539	4,716	7,260	8,495
ADJ. PAT	5,273	4,743	5,306	7,260	8,495
% chg	52.6	(10.0)	11.9	(5.8)	17.0
(% of Net Sales)	19.6	16.6	0.0	1.0	2.0
Basic EPS (₹)	25.5	22.9	22.0	30.2	35.3
Fully Diluted EPS (₹)	25.5	22.9	22.0	30.2	35.3
% chg	52.6	(10.0)	(3.7)	(18.9)	17.0

Balance Sheet (Consolidated)

Y/E March (₹ cr)	FY2014	FY2015	FY2016	FY2017E	FY2018E
SOURCES OF FUNDS					
Equity share capital	207	207	241	241	241
Preference capital	-	-	-	-	-
Reserves & surplus	18,318	26,300	31,164	38,142	46,355
Shareholders' funds	18,525	26,507	31,404	38,382	46,595
Minority interest	1,921	2,851	4,085	5,196	6,307
Total loans	2,561	7,596	8,338	8,338	8,338
Deferred tax liability	(911)	(1,752)	(2,126)	(2,126)	(2,126)
Other Long Term Liabilities	9	9	10	10	11
Long Term Provisions	2,602	2,710	2,293	2,221	2,480
Total liabilities	24,707	37,922	44,006	52,022	61,605
APPLICATION OF FUNDS					
Gross block	6,389	15,041	18,621	19,621	20,621
Less: Acc. depreciation	3,668	4,863	6,102	7,315	8,729
Net block	2,721	10,179	12,519	12,306	11,892
Capital work-in-progress	842	842	842	303	1,144
Goodwill	4,097	3,701	4,181	4,181	4,181
Investments	2,786	2,716	1,309	1,551	1,388
Long term long & adv.	1,051	2,736	3,032	3,402	3,854
Current assets	16,688	27,005	30,149	38,581	48,415
Cash	7,590	10,998	13,989	20,220	27,947
Loans & advances	3,774	2,193	2,006	2,480	2,481
Other	3,816	13,813	14,154	15,881	17,987
Current liabilities	3,477	9,256	8,026	8,302	9,269
Net current assets	13,211	17,748	22,123	30,279	39,147
Others	-	-	-	-	-
Total assets	24,707	37,922	44,006	52,022	61,605

Cash Flow Statement (Consolidated)

Y/E March (₹ cr)	FY2014	FY2015	FY2016	FY2017E	FY2018E
Profit before tax	7,098	6,641	7,356	9,838	11,300
Depreciation	409	1,195	1,014	1,214	1,414
(Inc)/Dec in working capital	(1,782)	(4,322)	(1,680)	(5,059)	(15,053)
Direct taxes paid	702	915	935	1,477	1,695
Cash Flow from Operations	5,024	2,598	5,754	4,515	(4,034)
(Inc.)/Dec.in Fixed Assets	681	(8,653)	(3,580)	(3,141)	(1,842)
(Inc.)/Dec. in Investments	(374)	70	1,408	1,165	163
Other income	-	-	-	-	-
Cash Flow from Investing	306	(8,583)	(2,172)	(1,975)	(1,679)
Issue of Equity	-	-	-	-	-
Inc./(Dec.) in loans	(548)	(4,928)	(1,157)	(1,230)	260
Dividend Paid (Incl. Tax)	(606)	-	(282)	(282)	(282)
Others	(645)	14,320	847	5,203	13,462
Cash Flow from Financing	(1,799)	9,392	(592)	(2,921)	13,440
Inc./(Dec.) in Cash	3,531	3,408	2,991	6,231	7,727
Opening Cash balances	4,059	7,590	10,998	13,989	20,220
Closing Cash balances	7,590	10,998	13,989	20,220	27,947

Key Ratios

Y/E March	FY2014	FY2015	FY2016	FY2017E	FY2018E
Valuation Ratio (x)					
P/E (on FDEPS)	26.8	29.8	31.0	22.6	19.4
P/CEPS	39.8	24.7	28.7	19.4	16.6
P/BV	7.6	6.2	4.5	3.7	3.0
Dividend yield (%)	0.4	0.4	0.1	0.1	0.1
EV/Sales	8.5	5.1	5.8	4.9	4.1
EV/EBITDA	19.7	17.7	22.0	15.4	12.6
EV / Total Assets	5.5	3.6	3.6	2.9	2.4
Per Share Data (₹)					
EPS (Basic)	25.5	22.9	22.0	30.2	35.3
EPS (fully diluted)	25.5	22.9	22.0	30.2	35.3
Cash EPS	17.1	27.7	23.8	35.2	41.2
DPS	2.5	3.0	1.0	1.0	1.0
Book Value	89.4	110.2	151.6	185.3	225.0
Dupont Analysis					
EBIT margin	40.7	24.3	24.4	29.8	30.4
Tax retention ratio	90.1	86.2	86.2	85.0	85.0
Asset turnover (x)	1.1	1.2	1.0	1.1	1.1
ROIC (Post-tax)	40.5	26.1	20.9	28.0	28.3
Cost of Debt (Post Tax)	2.9	9.8	5.2	5.1	9.7
Leverage (x)	0.0	0.0	0.0	0.0	0.0
Operating ROE	40.5	26.1	20.9	28.0	28.3
Returns (%)					
ROCE (Pre-tax)	32.0	21.1	16.6	18.9	18.9
Angel ROIC (Pre-tax)	57.4	38.3	28.6	38.4	38.6
ROE	32.3	21.1	18.3	20.0	20.1
Turnover ratios (x)					
Asset Turnover (Gross Block)	2.3	2.6	1.7	1.8	1.8
Inventory / Sales (days)	98	58	78	89	99
Receivables (days)	80	50	77	89	99
Payables (days)	49	61	94	72	72
WC cycle (ex-cash) (days)	91	82	96	92	57
Solvency ratios (x)					
Net debt to equity	(0.3)	(0.1)	(0.2)	(0.3)	(0.4)
Net debt to EBITDA	(0.7)	(0.4)	(0.8)	(1.2)	(1.7)
Interest Coverage (EBIT/Int.)	-	-	-	-	-

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Disclosure of Interest Statement

Sun Pharma

1. Financial interest of research analyst or Angel or his Associate or his relative	No
2. Ownership of 1% or more of the stock by research analyst or Angel or associates or relatives	No
3. Served as an officer, director or employee of the company covered under Research	No
4. Broking relationship with company covered under Research	No

Ratings (Based on expected returns over 12 months investment period):

Buy (> 15%)

Accumulate (5% to 15%)
Reduce (-5% to -15%)

Neutral (-5 to 5%)
Sell (< -15)