

## Institutional Equity Research

**Aurobindo Pharma**

Pharmaceuticals | India

4QFY17 Result Update | May 30, 2017

CMP* (Rs)	582
Upside/ (Downside) (%)	20.3
Bloomberg Ticker	ARBP IN
Market Cap. (Rs bn)	340
Free Float (%)	48
Shares O/S (mn)	584

**BUY** 

Target Price: Rs700

**US Business to Drive Growth**

Missing ours as well as street expectations, Aurobindo Pharma (ARBP) has delivered a weak performance in 4QFY17 with its Sales, EBITDA and PAT coming in at Rs36.4bn, Rs7.7bn and Rs5.6bn, respectively. Its overall revenue declined by 2.8% YoY due to weak Europe sales (-8% YoY to Rs 7.8bn) and ARV business (-20% YoY to Rs 2.6bn). Its US business remained flat on YoY comparison at Rs16.4bn due to price erosion in oral solids. Adjusting for one-off (Rs500mn) inventory write-off (Actavis EU biz) and exceptional items in other expenses and higher employee cost, its EBITDA margin declined 195bps YoY to 21.2%. Despite 11% YoY decline in EBITDA, ARBP's adjusted PAT grew by 3.4% YoY to Rs5.6bn primarily owing to lower tax rate (17.3% of PBT in 4QFY17 vs. 27.5% in 4QFY16). The Management has guided for positive growth in the US business in FY18 despite price erosion in high single-digit led by new product launches and low product concentration risk. **Considering likely growth in US business backed by strong growth in injectable portfolio and further margin improvement in European business (product transfers to India), we reiterate our BUY recommendation on the stock with a revised Target Price of Rs700.**

**Conference Call – Key Highlights**

- **US Biz (45% of Sales):** The Management expects the US business to witness price erosion (7-8% in FY17) over the next 4-6 quarters. However, it gave a strong commentary on the US business for FY18. ARBP's cumulative ANDA filings stand at 429 (final approval: 314; pending: 115). It launched 35 products in FY17 and plans to launch 20-25 products in FY18. ARBP mulls filing 12 oncology products in FY18 and looks forward to 4-5 approvals. The Management expects Natrol would contribute meaningfully to the US sales from 2HFY19 onwards.
- **Europe Biz (21% of Sales):** Management expects European business to grow by 5-8% YoY in FY18 with improvement in EBITDA margin led by product transfer to India.
- **Debt:** As of FY17, ARBP's total gross debt and cash in hand stood at US\$481mn and US\$80mn, respectively.
- **Key Guidance for FY18E:** Pegging the capex at ~US\$120mn (ex-vaccine and biosimilar), the Management expects the effective tax rate at ~25-26%; R&D spend at 6-7% of sales in FY18.

**Outlook & Valuation**

Looking ahead, we expect ARBP's US business to drive growth on the back of ramp-up in injectable products, incremental shifting of focus to high-growth/high-margin complex segment i.e. depot injections, micro- sphere, peptides, penem, ophthalmology, oncology and hormones, new launches and growth in Natrol business. **Based on the Management's strong commentary on US business despite price erosion in high single digit, while improved margins in European business, we reiterate our BUY recommendation on the stock with a revised Target Price of Rs700.**

Key Financials (Rs mn)	FY16	FY17	FY18E	FY19E
Sales	138,960	150,899	164,659	182,109
EBITDA	32,055	34,843	38,020	41,885
Adj. PAT	20,480	22,896	24,503	27,265
EPS (Rs)	35.1	39.2	42.0	46.7
P/E (x)	16.6	14.8	13.9	12.5
EV/Sales (x)	2.7	2.4	2.2	1.9
EV/EBITDA (x)	11.6	10.5	9.6	8.5
ROE (%)	29.0	24.8	21.2	19.3
ROCE (%)	18.0	18.6	16.9	16.2

Source: Company, RSec Research

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	(7.9)	(16.1)	(25.4)
Relative to Nifty	(11.1)	(24.0)	(42.8)

Shareholding Pattern (%)	Dec'16	Mar'17
Promoter	51.9	51.9
Public	48.1	48.1

**1 Year Stock Price Performance**

Note: \* CMP as on May 30, 2017

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## Risks to view

- Any inordinate delay in getting approval for new products in the US.
- Higher-than-expected price erosion in existing product portfolio.

## Exhibit 1: Segment-wise sales performance

(Rs mn)	4QFY17	4QFY16	YoY, %	3QFY17	QoQ, %
US	16,432	16,663	(1.4)	17,451	(5.8)
ARV	2,619	3,284	(20.2)	3,419	(23.4)
EU	7,772	8,407	(7.6)	8,554	(9.1)
ROW	1,971	1,756	12.2	1,878	5.0
Total Formulations	28,794	30,110	(4.4)	31,302	(8.0)
SSP+Cephalosporin	5121	5020	2.0	5250	(2.5)
ARV & others	2506	2726	(8.1)	2509	(0.1)
Total API	7627	7746	(1.5)	7759	(1.7)
Licensing income	-6	53	-	1	
Total	36,415	37,909	(3.9)	39,062	(6.8)
US (USD mn)	245	252	(2.9)	260	(5.8)

Source: Company, RSec Research

## Exhibit 2: Quarterly Performance

Y/E March (Rs mn)	4QFY17	4QFY16	YoY, %	3QFY17	QoQ, %
<b>Net Sales</b>	<b>36,416</b>	<b>37,459</b>	<b>(2.8)</b>	<b>39,062</b>	<b>(6.8)</b>
Cost of Revenues	15,028	16,259	(7.6)	17,097	(12.1)
Gross Profit	21,388	21,200	0.9	21,965	(2.6)
% of net sales	58.7	56.6	214	56.2	250
Employee expenses	4,635	4,068	13.9	4,456	4.0
Other Expenses	9,041	8,469	6.8	8,560	5.6
<b>Total operating expenses</b>	<b>28,704</b>	<b>28,796</b>	<b>(0.3)</b>	<b>30,113</b>	<b>(4.7)</b>
<b>EBITDA</b>	<b>7,712</b>	<b>8,663</b>	<b>(11.0)</b>	<b>8,948</b>	<b>(13.8)</b>
EBITDA margin (%)	21.2	23.1	(195)	22.9	(173)
Depreciation	1,001	1,113	(10.1)	1,111	(10.0)
<b>EBIT</b>	<b>6,712</b>	<b>7,550</b>	<b>(11.1)</b>	<b>7,837</b>	<b>(14.4)</b>
Other Income	218	210	3.4	79	174.6
Interest	143	251	(43.1)	143	0.1
<b>PBT</b>	<b>6,787</b>	<b>7,510</b>	<b>(9.6)</b>	<b>7,774</b>	<b>(12.7)</b>
Total tax	1,172	2,064	(43.2)	2,177	(46.2)
Tax Rate (%)	17.3	27.5		28.0	
Minority Interest	(19)	(1)	1,369.2	(31)	(38.4)
Adj PAT before extraordinary	5,634	5,448	3.4	5,628	0.1
Extraordinary items	309.7	(101.4)		(158.0)	
<b>Reported PAT</b>	<b>5,325</b>	<b>5,549</b>	<b>(4.0)</b>	<b>5,786</b>	<b>(8.0)</b>
Adj. EPS (Rs)	9.6	9.3	3.3	9.6	(0.0)

Source: Company, RSec Research

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### Profit & Loss Statement

Y/E March (Rs mn)	FY16	FY17	FY18E	FY19E
<b>Net sales</b>	<b>138,960</b>	<b>150,899</b>	<b>164,659</b>	<b>182,109</b>
% yoy change	14.6	8.6	9.1	10.6
<b>Adjusted RM cost</b>	<b>61,575</b>	<b>64,343</b>	<b>70,210</b>	<b>78,216</b>
Employee expenses	15,508	17,678	19,290	21,398
Other expenses	29,821	34,036	37,139	40,610
Total operating expenditure	106,905	116,056	126,638	140,224
<b>EBIDTA</b>	<b>32,055</b>	<b>34,843</b>	<b>38,020</b>	<b>41,885</b>
EBIDTA margin (%)	23.1	23.1	23.1	23.0
Depreciation	3,926	4,276	4,912	5,595
<b>EBIT</b>	<b>28,129</b>	<b>30,567</b>	<b>33,108</b>	<b>36,290</b>
Other income	682	538	538	538
Interest costs	927	667	624	581
<b>PBT</b>	<b>27,884</b>	<b>30,438</b>	<b>33,023</b>	<b>36,248</b>
Taxes	7,444	7,596	8,586	9,062
Tax rate (%)	26.7	25.0	26.0	25.0
Minority interest	(39)	(55)	(66)	(79)
<b>Adjusted PAT</b>	<b>20,480</b>	<b>22,896</b>	<b>24,503</b>	<b>27,265</b>
% yoy change	25.2	11.8	7.0	11.3
Exceptional item	660	0	0	0
<b>Reported PAT</b>	<b>19,820</b>	<b>23,017</b>	<b>24,503</b>	<b>27,265</b>
% yoy change	25.8	16.1	6.5	11.3
Adjusted EPS	35.1	39.2	42.0	46.7

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**Balance Sheet**

Y/E March (Rs mn)	FY16	FY17E	FY18E	FY19E
<b>SOURCES OF FUNDS</b>				
Equity Share Capital	585	586	586	586
Reserves& Surplus	69,983	91,629	114,761	140,655
Shareholders Funds	70,568	92,214	115,347	141,241
Minority Interest	596	21	(45)	(124)
Total Loans	40,762	30,841	28,841	26,841
<b>Total Liabilities</b>	<b>111,925</b>	<b>123,077</b>	<b>144,143</b>	<b>167,958</b>
<b>APPLICATION OF FUNDS</b>				
Gross Block	61,224	70,471	81,861	93,251
Less: Acc. Depreciation	19,713	23,989	28,901	34,496
Net Block	41,511	46,482	52,960	58,755
Capital Work-in-Progress	11,125	16,437	16,437	16,437
Investments	333	2,459	2,459	2,459
Current Assets	104,025	93,935	107,927	126,632
Cash	8,344	5,135	4,182	12,213
Loans & Advances	10,464	166	181	200
Other	85,217	88,634	103,564	114,218
Current liabilities	42,704	37,420	36,824	37,509
Net Current Assets	61,321	56,515	71,103	89,123
Net Deferred Tax	(2,364)	1,185	1,185	1,185
<b>Total Assets</b>	<b>111,925</b>	<b>123,077</b>	<b>144,143</b>	<b>167,958</b>

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**Cash Flow Statement**

Y/E March (Rs mn)	FY16	FY17E	FY18E	FY19E
Profit before tax	27,225	30,438	33,023	36,248
Depreciation	3,926	4,276	4,912	5,595
Interest provided	690	667	624	581
Change in Working Capital	7,383	(1,597)	15,541	9,989
Tax Paid	7,358	11,145	8,586	9,062
Others	50	-	-	-
<b>Cash Flow from Operations</b>	<b>17,694</b>	<b>25,435</b>	<b>14,432</b>	<b>23,372</b>
(Inc.) / Dec. in Fixed Assets	15,682	14,560	11,390	11,390
(Inc.) / Dec. in Investments	(260)	2,126	-	-
<b>Cash Flow from Investing</b>	<b>(13,763)</b>	<b>(16,686)</b>	<b>(11,390)</b>	<b>(11,390)</b>
Issue of Equity	72	1	-	-
Inc. / (Dec.) in loans	2,169	(9,921)	(2,000)	(2,000)
Dividend Paid (Incl. Tax)	1,342	1,371	1,371	1,371
Interest provided	(690)	(667)	(624)	(581)
<b>Cash Flow from Financing</b>	<b>(198)</b>	<b>(11,958)</b>	<b>(3,995)</b>	<b>(3,951)</b>
Inc. / (Dec.) in Cash	3,733	(3,209)	(953)	8,031
<b>Opening Cash balances</b>	<b>4,611</b>	<b>8,344</b>	<b>5,135</b>	<b>4,182</b>
<b>Closing Cash balances</b>	<b>8,344</b>	<b>5,135</b>	<b>4,182</b>	<b>12,213</b>

**Key Ratios**

Y/E March	FY16	FY17E	FY18E	FY19E
<b>Valuation Ratio (x)</b>				
P/E (on FDEPS)	16.6	14.8	13.9	12.5
P/CEPS	13.9	12.5	11.6	10.3
P/BV	4.8	3.7	2.9	2.4
Dividend yield (%)	0.4	0.3	0.3	0.3
EV/Sales	2.7	2.4	2.2	1.9
EV/EBITDA	11.6	10.5	9.6	8.5
EV / Total Assets	3.3	3.0	2.5	2.1
<b>Per Share Data (Rs)</b>				
Adjusted EPS	35.1	39.2	42.0	46.7
EPS (fully diluted)	35.1	39.2	42.0	46.7
Cash EPS	41.8	46.5	50.4	56.3
DPS	2.5	2.0	2.0	2.0
Book Value	120.8	157.9	197.5	241.9
<b>Returns (%)</b>				
RoCE	18.0	18.6	16.9	16.2
RoE	29.0	24.8	21.2	19.3
<b>Turnover ratios (x)</b>				
Asset Turnover (Gross Block)	2.3	2.1	2.0	2.0
Inventory / Sales (days)	107	105	115	120
Receivables (days)	110	67	85	85
Payables (days)	86	78	70	65
Working capital cycle (days)	131	93	130	140

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**Rating Guides**

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

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