

Steady improvement; upgrade to Buy

We upgrade Marksans Pharma (MPL) to Buy from Hold rating with a TP of Rs55 (earlier Rs45) based on 18x March'20E EPS of Rs3.0. MPL's Q3FY18 revenues and EBITDA were lower than our expectations but net profit was in-line with the expectations. The drug maker's Q3FY18 revenue grew 2% YoY, EBITDA margin improved 80bps to 13.3% and net profit grew 72% YoY. The Goa facility was approved by UK MHRA and TGA-Australia. We expect MPL's performance to improve led by the recent launch of four new products in the US and expected approvals for softgel capsules from US FDA. Key positive trigger to our assumption includes stupendous growth in the US market and key negative risk includes regulatory issues for the Goa facility from US FDA.

- **Revenue grew by 2%YoY:** MPL's revenues grew 2%YoY to Rs2.19bn from Rs2.15bn due to marginal growth in the UK and Europe. MPL's US and N. America business (42% of revenues) declined by 1% YoY to Rs923mn from Rs935mn. MPL's UK & Europe business (41% of revenues) grew by 5%YoY to Rs908mn from Rs864mn due to clearance of Goa facility by UK MHRA and TGA-Australia. The drug manufacturer's Australia and New Zealand business (11% of revenues) declined by 6% YoY due to lower off-take. We expect sales to grow, driven by US, and UK Europe businesses.
- **Margin improved 80bps YoY:** MPL's EBITDA margin improved by 80bps YoY to 13.3% from 12.5% due to the reduction in material cost and personnel cost. Material cost declined by 360bps to 52.3% from 55.9% due to the change in the product mix. Personnel cost declined by 130bps YoY to 16.5% from 17.8%. Other expenses grew by 390bps YoY to 17.8% from 13.9% due to Rs50mn forex loss in Q3FY18 against nil in Q3FY17. We expect margins to improve from strong growth in its products in the US, UK and Europe and additional ANDA approvals from US FDA.
- **Net profit grew by 72%YoY:** MPL's net profit for the quarter grew by 72%YoY to Rs172mn from Rs100mn due to margin improvement and lower depreciation. We expect the company to report sustainable growth, driven by the US, UK and EU businesses and commencement of the domestic formulation business.
- **Recommendation and key risks:** We have revised our FY18E and FY19E EPS downwards by 3% and 19% respectively. We upgrade MPL to Buy from Hold rating, with a TP of Rs55 based on 18x March'20E EPS of Rs3.0, and a 45.3% upside from CMP. Key positive upsides would be additional ANDA approvals from US FDA and key negative would be regulatory issue with US FDA for its Goa facility.

Particulars (Rs mn)	Q3FY18	Q3FY17	YoY Gr%	Q2FY18	QoQ Gr %	Q3FY18E	% Var.
Total Sales	2,188	2,152	1.7	2,738	(20.1)	2,915	(24.9)
Other expenses	390	299	30.4	370	5.4	390	0.0
as % of total income	17.8	13.9		13.5		13.4	
Total Expenditure	1,896	1,884	0.6	2,493	(23.9)	2,560	(25.9)
EBITDA	292	268	9.0	245	19.2	355	(17.7)
EBITDA Margin (%)	13.3	12.5		8.9		12.2	
PBDIT	296	268	10.4	245	20.8	355	(16.6)
Depreciation	62	118	(47.5)	70	(11.4)	80	(22.5)
PBT	216	132	63.6	145	49.0	243	(11.1)
Prov. For tax	37	16	131.3	41	(9.8)	55	(32.7)
% of PBT	17.1	12.1		28.3		22.6	
PAT before minority interest	179	116	54.3	104	72.1	188	(4.8)
Minority interest	7	16	(56.3)	10	NA	13	(46.2)
Reported PAT	172	100	72.0	94	83.0	175	(1.7)

Source: Company, Centrum Research Estimates

Target Price	Rs55	Key Data	
CMP*	Rs38	Bloomberg Code	MRKS IN
Upside	45.3%	Curr Shares O/S (mn)	409.3
Previous Target	Rs45	Diluted Shares O/S(mn)	409.3
Previous Rating	Hold	Mkt Cap (Rsbn/USDmn)	15.5/239.4
Price Performance (%)*		52 Wk H / L (Rs)	58.3/34.2
		5 Year H / L (Rs)	115/3.4
MRKS IN	(14.6)	(0.3)	(22.0)
Nifty	(4.9)	5.3	16.7
		Daily Vol. (3M NSE Avg.)	5848558

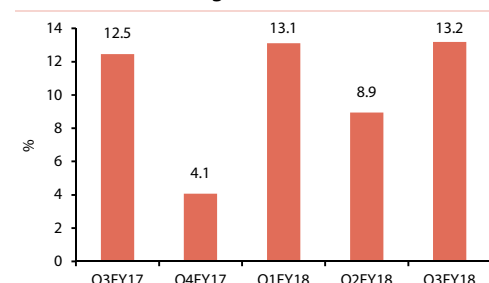
Source: Bloomberg, Centrum Research, *as on 19th February 2018

Shareholding pattern* (%)

	Dec-17	Sept-17	Jun-17	Mar-17
Promoter	48.3	48.3	48.3	48.2
FII's	2.3	7.7	8.5	8.4
DII's	2.8	0.4	0.3	0.3
Others	46.6	43.6	42.9	43.1

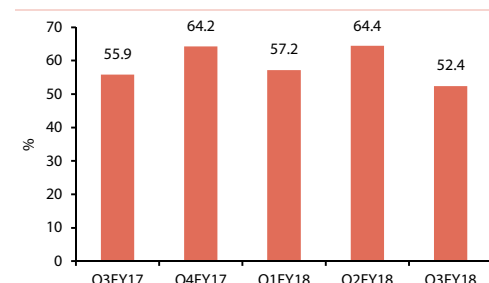
Source: BSE, *as on 19th February 2018

Trend in EBITDA margin (%)



Source: Company, Centrum Research

Trend in Material cost (%)



Source: Company, Centrum Research

Earning Revision

Particulars (Rs mn)	FY18E			FY19E		
	New	Old	Chg (%)	New	Old	Chg (%)
Revenue	9,520	10,296	(7.5)	11,033	12,152	(9.2)
EBITDA	1,095	1,131	(3.2)	1,474	1,698	(13.2)
EBITDA Margin (%)	11.5	11.0	50bps	13.4	14.0	(60)bps
PAT	529	547	(3.3)	815	1,009	(19.2)

Source: Centrum Research Estimates

Ranjit Kapadia, ranjit.kapadia@centrum.co.in; 91 22 4215 9645

Y/E Mar (Rsmn)	Revenue	YoY (%)	EBITDA	EBITDA (%)	Adjust. PAT	YoY (%)	DEPS Rs.	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
FY16	8,933	12.1	1,363	15.3	784	(28.3)	1.9	19.4	17.7	40.9	24.0
FY17	7,672	(14.1)	444	5.8	94	(88.0)	0.2	2.2	2.9	198.5	44.3
FY18E	9,520	24.1	1,095	11.5	529	461.8	1.3	11.4	10.2	33.7	17.5
FY19E	11,033	15.9	1,474	13.4	815	54.1	2.0	15.4	13.1	19.1	11.0
FY20E	13,131	19.0	2,000	15.2	1,232	51.1	3.0	19.8	16.9	12.6	8.2

Source: Company, Centrum Research Estimate

In the interest of timeliness, this document is not edited

Centrum Equity Research is available on Bloomberg, Thomson Reuters and FactSet

Sales composition

MPL's Q3FY18 sales composition was as follows:

MPL's revenue grew by 2% YoY to Rs2.19bn from Rs2.15bn due to the absence of new launches in UK and US markets. The company's UK, Europe revenues (41% of sales) grew by 5% YoY to Rs908mn from Rs864mn. The company's RoW revenues (6% of sales) grew by 18% YoY to Rs122mn from Rs103mn.

The US business (42% of sales) declined by 1% YoY to Rs923mn from Rs935mn due to the absence of new launches. The company's Australia & New Zealand business (11% of revenues) declined by 6% YoY to Rs235mn from Rs250mn due to lower off-take. We expect the US and UK, Europe businesses to drive future growth.

Exhibit 1: Geography-wise revenues (consolidated)

PARTICULARS (Rs mn)	Q3FY18	Q3FY17	YoY Gr%	Q2FY18	QoQ Gr %	Q3FY18E	% Var.
Europe, UK-formulations	908	864	5.1	1,331	(31.8)	1,450	(37.4)
US, N.America-formulations	923	935	(1.3)	1,027	(10.1)	1,100	(16.1)
Australia, NZ-formulations	235	250	(6.0)	280	(16.1)	260	(9.6)
RoW formulations	122	103	18.4	100	22.0	105	16.2
Other op. income	0	0		0			
Total Revenues	2,188	2,153	1.6	2,738	(20.1)	2,915	(24.9)

Source: Company

Other developments

US business-likely to improve

- MPL's US business' (42% of revenues) declined by 1%YoY to Rs923mn from Rs935mn.
- MPL has commenced marketing of the following products in the US after receiving approvals from US FDA: Metformin HCl ER tablets 500 and 750mg, Paricalcitol softgel capsules 1, 2 and 4 mcg, Loratidine softgel capsules 10mg and Dutasteride softgel capsules 0.5mg. Paricalcitol softgel capsules and Dutasteride softgel capsules have limited competition whereas Loratidine softgel has no competition from other generic players.
- The company is currently marketing 13 approved products in the US and awaiting further approval from the eight pending ANDAs with US FDA.
- The company did not witness any price erosion for its products in the US generic market.

UK, Europe business-Goa facility cleared by UK MHRA

- The company's UK & Europe business (41% of sales) grew by 5% YoY to Rs908mn from Rs864mn due to commencement of despatches after clearance of Goa facility by UK MHRA.
- During FY17, sales to UK and Europe was impacted by restrictive import of critical products in the UK by UK MHRA.

Australia, NZ-business declined by 6% YoY

- MPL's Australia, NZ business (11% of revenues) declined by 6%YoY to Rs235mn from Rs250mn due to lower off take of its products.
- The Goa facility was inspected by TGA-Australia in FY17 and cleared without any observations.

IT initiatives and automation

- MPL has incorporated state-of-the-art IT applications in Quality, Manufacturing and R&D functions with laboratory automation, instrument integration and manufacturing execution and spent ~Rs80mn on the same in FY17.
- The company has established a new R&D centre in Nerul for formulation development and NDDS for regulated markets and has recruited 15 scientists. The major work would involve the preparation of dossiers for the regulated markets. The R&D centre is functional and is expected to have 50 scientists by end of FY18.

- MPL has plans to generate a pipeline of over 30 products for the regulated markets by FY20.
- The company generates over 95% of its revenues from the regulated markets of the US, EU, Australia/NZ and Canada.
- MPL has entered into the branded generic business in the domestic market with over 45 brands in dermatology, respiratory and CNS segments. The revenues are likely to accrue from Q4FY18 onwards.
- MPL's Goa facility received Form 483 from UK MHRA with 4 observations in April'17. The company has responded to these observations.
- The company has received EIR for its Goa facility from UK MHRA and has commenced supplies to UK and EU markets.

Earnings revision

Based on Q3FY18 results, we have revised our FY18E and FY19E EPS downwards by 3% and 19% respectively in view of increase in crude based raw material prices. The company's Goa facility has received Form 483 from UK MHRA with 4 observations in April'17, which were responded by the company. MPL received EIR for its Goa facility from UK MHRA in Sept'17. We expect MPL's performance to improve, with good growth expected in the US market from the recent launch of four products in the US and six pending ANDA approvals for softgel capsules. The UK and EU business has normalised after EIR from UK MHRA for its Goa facility. We upgrade MPL to Buy from Hold rating, with a TP of Rs55 based on 18x March'20E EPS of Rs3.0, and a 45.3% upside from CMP. Key positive upsides for MPL would be pending ANDA approvals from US FDA and key negative would be regulatory issue with US FDA for its Goa facility.

Exhibit 2: Earnings revision

Particulars	FY18E			FY19E		
	Current	Earlier	Chg(%)	Current	Earlier	Chg(%)
Sales	9,520	10,296	(7.5)	11,033	12,152	(9.2)
EBIDTA	1,095	1,131	(3.2)	1,474	1,698	(13.2)
EBIDTA margin (%)	11.5	11.0	50bps	13.4	14.0	(60)bps
Net profit	529	547	(3.3)	815	1,009	(19.2)

Source: Centrum Research Estimates

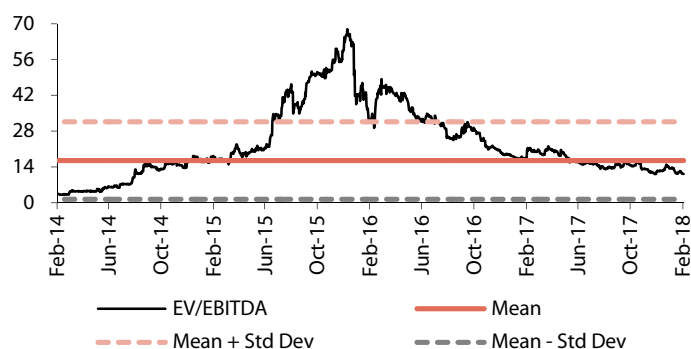
Valuation and recommendation

Exhibit 3: Sensitivity Analysis

Sensitivity to key variables – FY18E	% change	% impact on EBITDA	% impact on EPS
Sales	1	8.7	18.0
Material cost	1	(5.1)	(10.6)

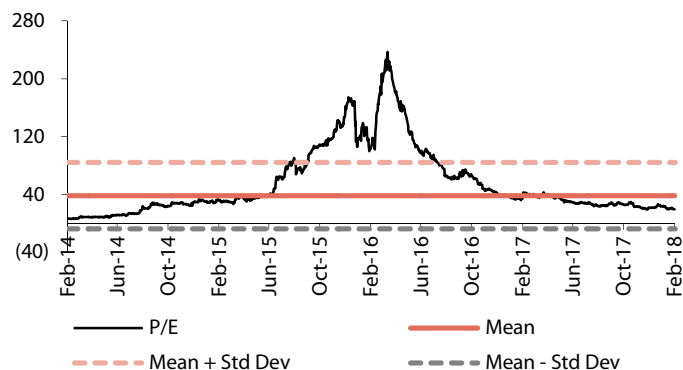
Source: Company, Centrum Research Estimates

Exhibit 4: 1 year forward EV/EBITDA chart



Source: Bloomberg, Company, Centrum Research Estimates

Exhibit 5: 1 year forward P/E chart



Source: Bloomberg, Company, Centrum Research Estimates

Exhibit 6: Comparative Valuations

Company	Mkt Cap (Rs mn)	CAGR FY17-FY19E (%)			EBITDA Margin (%)			PE (x)			EV/EBITDA (x)			RoE (%)			Div Yield (%)		
		Rev.	EBITDA	PAT	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E	FY17	FY18E	FY19E
Marksans Pharma	15,554	19.9	82.2	194.4	5.8	11.5	13.4	198.5	33.7	19.1	44.3	17.5	11.0	2.2	11.4	15.4	0.4	0.4	0.5
Granules India	29,210	21.0	18.7	20.9	20.8	19.3	20.0	20.3	19.2	12.8	10.5	9.5	6.8	20.0	13.2	15.3	0.8	0.9	1.2
Strides Shasun*	65,629	4.6	5.7	(6.8)	18.8	14.7	19.2	21.9	32.6	16.7	17.1	16.5	11.7	16.6	6.6	12.6	0.4	0.8	1.0
Unichem Labs *	29,796	(18.9)	(69.9)	(55.3)	11.8	(7.3)	1.6	22.4	(29.8)	211.4	14.1	(9.1)	186.7	10.8	(2.6)	0.4	0.7	0.8	0.8

Source: Company, Centrum Research Estimates, *Bloomberg Estimates Prices as on 19th February 2018

Quarterly financials, Operating Metrics and Key Performance Indicators

Exhibit 7: Quarterly Financials

Particulars (Rs mn)	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18
Total Sales	2,102	1,868	1,804	2,152	1,848	2,211	2,738	2,184
Materials Cost	1,448	1,098	1,100	1,202	1,187	1,264	1,763	1,144
Personnel expenses	311	383	352	383	383	374	360	362
Other expenses	300	252	349	299	202	283	370	390
Total Expenditure	2,059	1,733	1,801	1,884	1,772	1,921	2,493	1,896
EBIDTA	43	135	3	268	75	290	245	288
Other income	65	0	67	0	2	0	0	4
PBDIT	108	135	70	268	77	290	245	292
Depreciation	84	48	59	118	76	74	70	62
Interest	20	13	11	18	16	19	30	18
PBT	4	74	0	132	(14)	197	145	212
Tax	44	21	(9)	16	19	52	41	37
PAT before minority	(39)	53	9	116	(33)	145	104	175
Minority interest	18	9	1	16	(0)	8	10	7
PAT after minority	(58)	44	8	100	(33)	137	94	168
Growth Rates %								
Sales	21.0	(11.1)	(29.4)	(1.0)	(12.1)	18.4	51.8	1.5
EBIDTA	(89.7)	(73.1)	(99.4)	(12.1)	74.7	115.1	8,066.7	7.5
Net profit	(123.0)	(85.9)	(97.7)	(44.3)	(42.4)	208.6	1,075.0	68.0
Margin %								
EBIDTA margin	2.1	7.2	0.2	12.5	4.1	13.1	8.9	13.2
PBT margin	0.2	4.0	0.0	6.1	(0.8)	8.9	5.3	9.7
Net margin	(2.7)	2.4	0.4	4.6	(1.8)	6.2	3.4	7.7

Source: Company, Centrum Research

Exhibit 8: Key performance indicators

Key performance indicator	FY16	FY17	FY18E	FY19E	FY20E
Sales gr. Rate%	12.1	(14.1)	24.1	15.9	19.0
Material cost %	57.1	59.8	58.5	57.7	56.8

Source: Company, Centrum Research Estimates

Financials -consolidated

Exhibit 9: Income Statement

Y/E March	FY16	FY17	FY18E	FY19E	FY20E
Revenues	8,933	7,672	9,520	11,033	13,131
Material cost	5,097	4,588	5,565	6,370	7,455
% of revenues	57.1	59.8	58.5	57.7	56.8
Employee cost	1,224	1,501	1,475	1,625	1,910
% of revenues	13.7	19.6	15.5	14.7	14.5
Other Expenses	1,249	1,139	1,385	1,564	1,766
% of revenues	14.0	14.8	14.5	14.2	13.4
EBIDTA	1,363	444	1,095	1,474	2,000
EBIDTA margin (%)	15.3	5.8	11.5	13.4	15.2
Depreciation & Amortisation	281	301	286	324	358
EBIT	1,082	143	809	1,150	1,643
Interest Expenses	102	57	85	80	70
PBT from operations	980	86	724	1,070	1,573
Other income	89	69	10	20	30
PBT	1,068	154	734	1,090	1,603
Tax provision	242	35	175	240	330
Effective tax rate (%)	22.7	22.7	23.8	22.0	20.6
Net profit	826	119	559	850	1,273
Minority interest	42	25	30	35	40
Reported net profit	784	94	529	815	1,232
Adj. Net profit	784	94	529	815	1,232

Source: Company, Centrum Research Estimates

Exhibit 10: Key Ratios

Y/E March	FY16	FY17	FY18E	FY19E	FY20E
Growth Ratios (%)					
Revenues	12.1	(14.1)	24.1	15.9	19.0
EBIDTA	(26.2)	(67.4)	146.8	34.6	35.7
Adj. Net Profit	(28.3)	(88.0)	461.8	54.1	51.1
Margin Ratios (%)					
EBIDTA margin	15.3	5.8	11.5	13.4	15.2
PBT from operations margin	11.0	1.1	7.6	9.7	12.0
Adj. PAT margin	8.8	1.2	5.6	7.4	9.4
Return Ratios (%)					
RoCE	17.7	2.9	10.2	13.1	16.9
RoE	19.4	2.2	11.4	15.4	19.8
RoIC	20.9	2.1	10.6	14.1	18.6
Turnover ratios (days)					
Gross Block Turnover (x)	2.5	1.8	2.1	2.3	2.6
Debtors	89	118	119	112	122
Creditors	49	77	65	69	64
Inventory	69	90	95	89	91
Cash Conversion Cycle	109	131	148	132	149
Solvency Ratio					
Debt-Equity	0.2	0.3	0.3	0.3	0.2
Net Debt-Equity	0.1	0.2	0.3	0.1	0.1
Current Ratio	2.6	2.5	2.8	2.7	2.9
Interest Coverage Ratio	0.1	0.4	0.1	0.1	0.0
Gross Debt/EBIDTA	0.7	2.7	1.6	1.0	0.8
Per Share (Rs)					
FDEPS (adjusted)	1.9	0.2	1.3	2.0	3.0
CEPS	2.6	1.0	2.0	2.8	3.9
Book Value	11.1	10.9	12.0	13.8	16.6
Dividend	0.12	0.12	0.15	0.15	0.2
Dividend Payout (%)	8.6	70.6	13.6	8.8	7.8
Valuations (x) (Avg Mkt Cap)					
PER	40.9	198.5	33.7	19.1	12.6
P/BV	7.1	4.2	3.6	2.7	2.3
EV/EBIDTA	24.0	44.3	17.5	11.0	8.2
Dividend Yield (%)	0.2	0.4	0.4	0.5	0.6
5-yr Avg AOCF/EV yield(%)	1.1	2.7	2.2	3.2	1.7

Source: Company, Centrum Research Estimates

Exhibit 11: Balance Sheet

Y/E March	FY16	FY17	FY18E	FY19E	FY20E
Share capital	409	409	409	409	409
Reserves & surplus	4,009	3,928	4,507	5,251	6,388
Total shareholders Funds	4,418	4,337	4,917	5,660	6,797
Total Debt(incl. Pref.cap)	1,004	1,207	1,700	1,500	1,600
Minority interest	84	62	70	80	81
Deferred tax Liab.	(19)	(3)	(7)	(5)	(20)
Total Liabilities	5,487	5,603	6,680	7,235	8,458
Gross Block	4,241	4,453	4,672	4,942	5,192
Less: Acc. Depreciation	1,544	1,780	2,006	2,260	2,537
Net Block	2,697	2,673	2,666	2,682	2,655
Capital WIP	-	-	-	-	-
Net Fixed Assets	2,697	2,673	2,666	2,682	2,655
Investments	-	-	-	-	-
Inventories	1,678	1,901	2,470	2,700	3,270
Debtors	2,173	2,476	3,100	3,400	4,400
Loans & Advances	303	219	315	370	425
Cash & Bank Balance	352	251	359	820	819
Other assets	-	-	-	-	-
Total Current Assets	4,506	4,847	6,244	7,290	8,914
Trade payable	1,190	1,618	1,700	2,100	2,300
Other current Liabilities	7	7	10	15	20
Provisions	519	291	521	622	791
Net Current Assets	2,790	2,930	4,013	4,553	5,803
Total Assets	5,487	5,603	6,680	7,235	8,458

Source: Company, Centrum Research Estimates

Exhibit 12: Cash Flow

Y/E March	FY16	FY17	FY18E	FY19E	FY20E
CF before WC changes	1,189	376	826	1,152	1,594
Working Capital Changes	(881)	(241)	(975)	(79)	(1,251)
CF from Operations	308	135	(149)	1,073	343
Adj OCF (OCF-Interest)	270	78	(234)	993	273
Change in fixed assets	(1,319)	(277)	(279)	(340)	(330)
Adj. FCF (AOCF-Capex)	(1,049)	(199)	(513)	653	(57)
CF from Investing	(1,230)	(277)	(279)	(340)	(330)
CF from Financing	(578)	152	531	(272)	4
Net change in Cash	(1,500)	9	104	461	17

Source: Company, Centrum Research Estimates

Appendix A

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Marksans Pharma price chart



Source: Bloomberg, Centrum Research

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		Granules India	Marksans Pharma
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Hold	Upside between -20% to +20%	Upside between -15% to +15%	Upside between -10% to +10%
Sell	Downside > 20%	Downside > 15%	Downside > 10%

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PORTFOLIO MANAGER

SEBI REGN NO.: INP000004383

Website: www.centrum.co.in

Investor Grievance Email ID: investor.grievances@centrum.co.in

Compliance Officer Details:

Kavita Ravichandran

(022) 4215 9842; Email ID: Compliance@centrum.co.in

Centrum Broking Ltd. (CIN :U67120MH1994PLC078125)

Registered Office Address	Corporate Office & Correspondence Address
Bombay Mutual Building , 2nd Floor, Dr. D. N. Road, Fort, Mumbai - 400 001	Centrum House 6th Floor, CST Road, Near Vidya Nagari Marg, Kalina, Santacruz (E), Mumbai 400 098. Tel: (022) 4215 9000