

Aurobindo Pharma

BSE SENSEX 37,869
S&P CNX 11,430

CMP: INR610 TP: INR750 (+23%)

Buy

Motilal Oswal values your support in the Asiamoney Brokers Poll 2018 for India Research, Sales and Trading team. We request your ballot.



Bloomberg	ARBP IN
Equity Shares (m)	586
M.Cap.(INRb)/(USD\$b)	357.5 / 5.2
52-Week Range (INR)	809 / 527
1, 6, 12 Rel. Per (%)	-6/-8/-31
12M Avg Val (INR M)	1782
Free float (%)	48.1

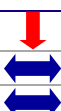
Financials & Valuations (INR b)

Y/E Mar	2018	2019E	2020E
Net Sales	165.0	183.3	204.6
EBITDA	37.9	40.3	45.6
PAT	25.0	25.9	29.0
EPS (INR)	42.7	44.2	49.5
Gr. (%)	8.7	3.5	11.9
BV/Sh (INR)	199.4	240.0	287.0
RoE (%)	23.8	20.1	18.8
RoCE (%)	17.4	15.3	15.2
P/E (x)	14.3	13.8	12.3
P/BV (x)	3.1	2.5	2.1

Estimate change

TP change

Rating change



Margins subdued, but outlook intact

- **Lower gross margin leads to earnings miss:** Aurobindo Pharma's (ARBP) revenue grew ~16% YoY to INR42.5b (est. of INR42b), largely led by growth of 30% YoY in EU (34% of sales), 32% YoY in growth market (7% of sales) and 20% YoY in API (21% of sales). US sales continued the uptrend, with 11.5% YoY growth to INR19b (54% of sales). Gross margin shrank 420bp YoY to 55.1% due to provision related to product recall, a change in product mix and increased raw material prices. EBITDA margin shrank ~450bp YoY (-150bp QoQ) to 18.3% due to gross margin contraction and higher employee cost. EBITDA declined ~7.4% YoY to INR7.8b (est. of INR9.2b). Reported PAT was lower at INR4.5b due to a forex loss of INR682m. Adjusting for the same, PAT would be INR5.2b.
- **US sales continue uptrend; strong growth momentum in EU:** US sales came in at USD282m (+7% YoY, 4% QoQ). Injectable sales stood at USD36m (v/s USD32m in 4Q), while Natrol sales were stable YoY at USD34m. EU sales grew 16% YoY on a CC basis. ARBP has transferred manufacturing of 94 products from EU to India, and is on track to improve its operating margins.
- **Key con-call takeaways:** (1) Although 1QFY19 US injectable sales were subdued, ARBP remains confident to grow by 30% YoY on USD163m sales in FY18. (2) Net debt increased by USD33m sequentially due to an increase in working capital (up USD63m) and capex of USD70m. (3) ARBP filed first derma ANDA this quarter; is on track to file 10-12 ANDAs in this space. (4) Apotex deal would be complete by 3QFY19. (5) A few ANDAs expected in FY19 are g-Toprol, g-Prevacid and g-Welchol.
- **Valuation and view:** We cut our FY19/FY20 EPS estimates by 9%/7% to INR44.2/INR49.5 to factor in increased raw material prices. We roll our target to 15x 12M forward earnings and arrive at a TP of INR750. We remain positive on ARBP on the back of its strong ANDA pipeline, consistency in compliance and robust growth in EU business. Maintain **Buy**.

Quarterly perf. (Consol.)

Y/E March	FY18				FY19E				FY18	FY19E	(INR M)	
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			FY18E	
Net Sales	36,788	44,359	43,361	40,491	42,503	45,224	48,024	47,523	164,998	183,259	42,026	1.1%
YoY Change (%)	-2.3	17.5	11.0	11.2	15.5	2.0	10.8	17.4	9.3	11.1	14.2	
EBITDA	8,416	11,173	10,256	8,040	7,792	9,633	11,045	11,861	37,885	40,317	9,246	-15.7%
Margins (%)	22.9	25.2	23.7	19.9	18.3	21.3	23.0	25.0	23.0	22.0	22.0	
Depreciation	1,312	1,321	1,381	1,566	1,545	1,550	1,550	1,541	5,580	6,186	1,465	
Interest	169	173	189	247	295	214	214	133	777	856	214	
Other Income	221	103	258	438	437	125	125	113	1,020	800	125	
PBT before EO expense	7,156	9,782	8,944	6,665	6,389	7,994	9,406	10,301	32,548	34,075	7,692	
Extra-Ord expense	77	4	-73	159	682	0	0	0	168	682	0	
PBT	7,080	9,778	9,017	6,506	5,707	7,994	9,406	10,301	32,380	33,393	7,692	
Tax	1,910	1,980	3,069	1,224	1,155	1,998	2,399	2,625	8,183	8,178	1,923	
Rate (%)	27.0	20.2	34.0	18.8	20.2	25.0	25.5	25.5	25.3	24.5	25.0	
Minority Interest	-15	-13	-3	-3	-3	-14	-14	-24	-34	-55	-14	
Reported PAT	5,185	7,812	5,950	5,285	4,555	6,009	7,022	7,684	24,231	25,270	5,782	-21.2%
Adj PAT	5,226	7,802	6,564	5,429	5,182	6,009	7,022	7,684	25,021	25,897	5,769	-9.8%
YoY Change (%)	-9.7	32.0	2.9	-2.7	-0.4	-23.2	6.8	41.8	10.9	3.5	10.4	
Margins (%)	14.2	17.6	15.1	13.4	12.2	13.3	14.6	16.2	15.2	14.1	13.7	

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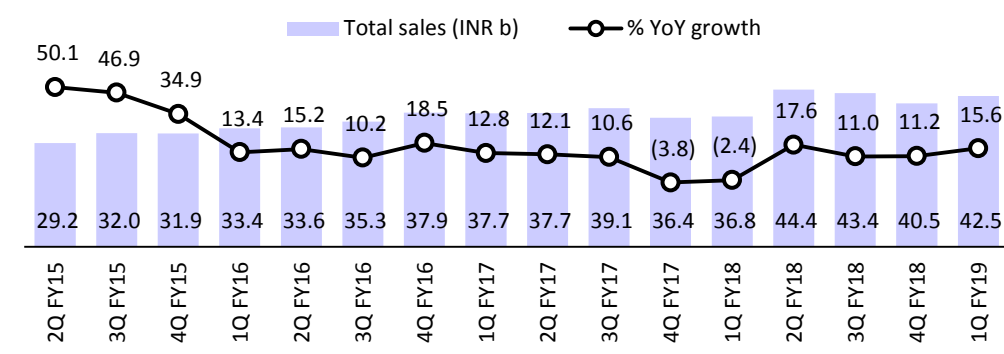
Investors are advised to refer through important disclosures made at the last page of the Research Report.

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Business highlights

ARBP 1QFY19 revenues reported healthy growth of ~16% YoY to INR42.5b. Formulation segment (82% of sales), reported growth of ~15% YoY to INR35b, primarily led by significant growth in the Europe and RoW market (~34% of sales) by ~31% YoY to INR14.6b and healthy growth in the US business (~45% of sales) by ~12% YoY to INR18.9b. ARV business continued to decline by ~36% YoY to INR1.5b. API business (~18% of sales) increased by ~18% to INR 7.5b.

Exhibit 1: Revenue increased 16% YoY in 1QFY19

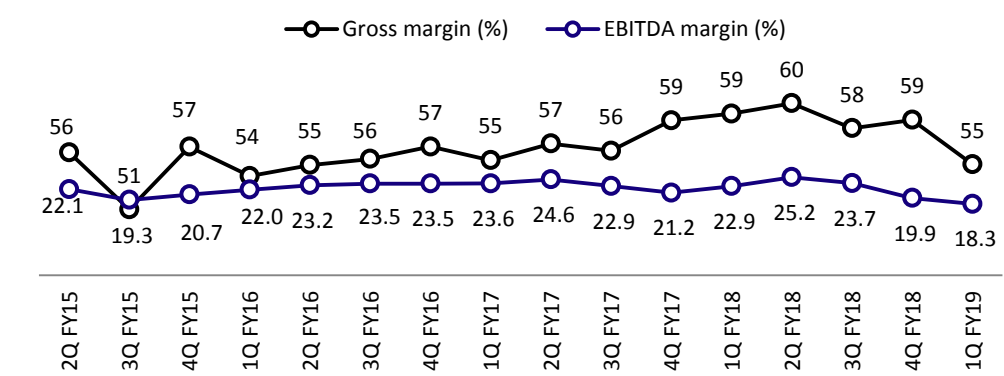


Source: Company, MOSL

Lower gross margin drags overall profitability

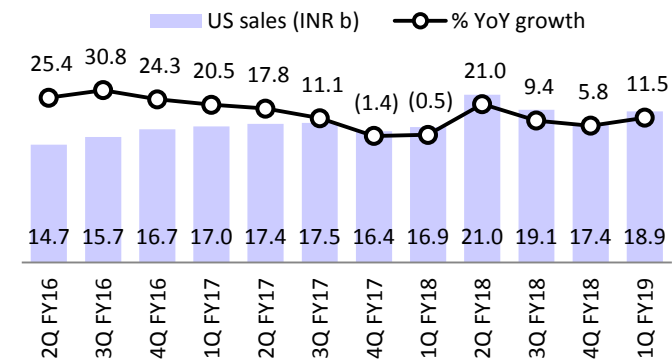
Despite healthy revenue growth, EBITDA declined by ~7% YoY to INR7.8b (v/s est. of INR9.2b). This is primarily due to decline in gross margin to ~55% from 59% in 1QFY18. Provision of raw material of ~INR1b, product re-call and change in product mix led to fall in gross margin. EBITDA margin also fell in line with gross margin to 18.3% from 22.9% in 1QFY18. Increase in employee expense by ~70bp YoY (as % of sales) was off-set by lower R&D spend by ~40bp YoY (as % of sales).

Exhibit 2: Gross and EBITDA margin declined YoY

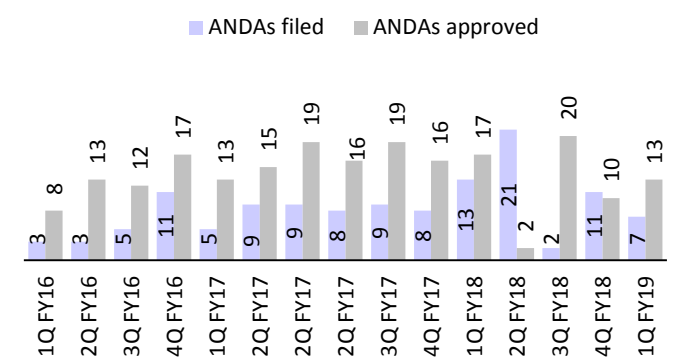


Source: Company, MOSL

US business growth remains on uptrend (~45% of sales): US business grew by ~12% YoY and ~9% QoQ to INR18.9b. Although growth injectable business was subdued, company is confident of growing 30% in FY19, with growth kicking in from 2QFY19. ARBP expects growth momentum to continue over next 12-18 months on the back of launches in injectable space and other key launches like gToprol and gPrevacid

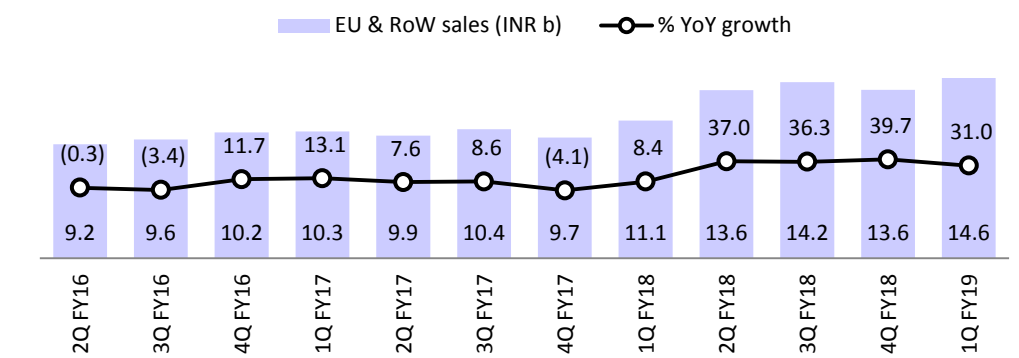
Exhibit 3: US business grew by ~12% YoY

Source: Company, MOSL

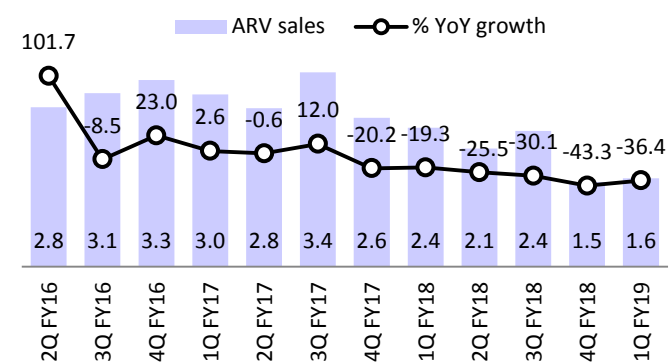
Exhibit 4: ANDA filed v/s approved (quarterly trend)

Source: Company, MOSL

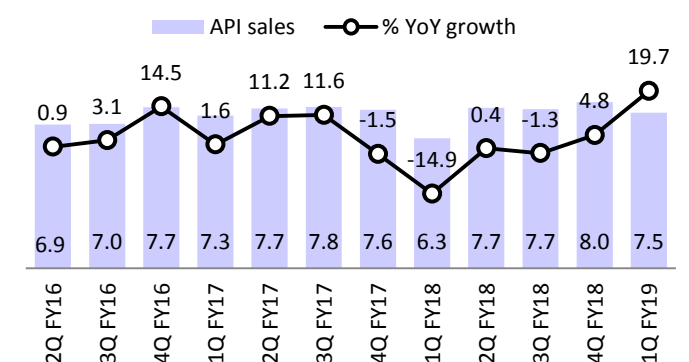
Growth momentum continues in Europe and RoW market (34% of sales): In 1QFY19, Europe and RoW combined increased by ~31% YoY to INR14.6b on back of healthy growth across geographies in the respective regions. Europe business grew ~31% YoY to INR12b while RoW market grew ~32%YoY to INR2.6b. Margins in Europe are on increasing trend on back of outsourcing of products to Indian facility

Exhibit 5: Increasing growth trend in EU and RoW continues

Source: Company, MOSL

Exhibit 6: ARV sales continues to decline

Source: Company, MOSL

Exhibit 7: API sales reported healthy growth of ~20% YoY

Source: Company, MOSL

Operating metrics

Exhibit 8: Key operating metrics

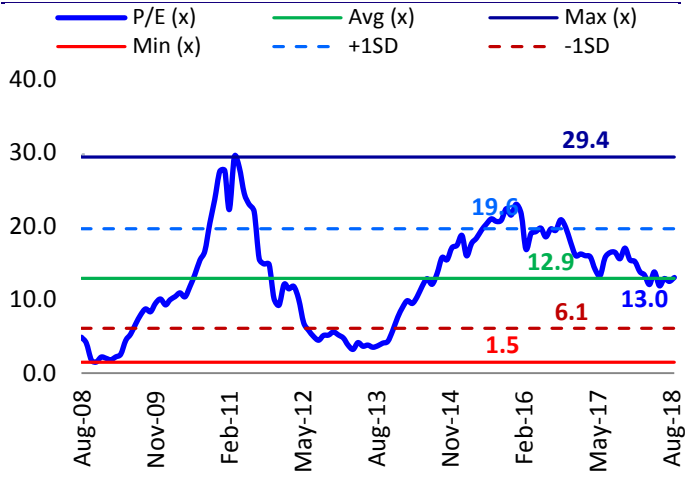
	1QFY16	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19
Revenue Mix (%)													
Formulations	78.3	79.5	80.3	79.5	80.5	79.6	80.1	79.1	83.0	82.6	82.3	80.2	82.4
ARV form.	8.8	8.3	8.6	8.7	8.0	7.4	8.8	7.2	6.7	4.7	5.5	3.7	3.7
US generic form.	42.3	43.8	44.5	44.0	45.2	46.0	44.7	45.1	46.1	47.3	44.0	42.9	44.5
EU and ROW form.	27.2	27.4	27.2	26.8	27.2	26.2	26.7	26.8	30.2	30.6	32.8	33.6	34.3
APIs	21.7	20.5	19.7	20.5	19.5	20.4	18.7	20.9	17.0	17.4	17.7	19.7	17.6
Betalactum	14.3	12.7	12.7	13.3	13.1	13.6	11.8	14.1	11.1	11.6	12.4	13.2	11.6
Non Betalactum	7.3	7.8	7.0	7.2	6.4	6.8	6.9	6.9	5.9	5.8	5.3	6.6	6.0
Revenue Growth (%)													
Formulations	15.0	19.5	12.1	19.6	15.9	12.4	10.3	(4.4)	0.6	22.0	14.1	12.8	14.7
ARV form.	31.7	101.7	(8.5)	23.0	2.6	(0.6)	12.0	(20.2)	(19.3)	(25.5)	(30.1)	(43.3)	(36.4)
US generic form.	26.7	25.4	30.8	24.3	20.5	17.8	11.1	(1.4)	(0.5)	21.0	9.4	5.8	11.5
EU and ROW form.	(3.0)	(0.3)	(3.4)	11.7	13.1	7.6	8.6	(4.1)	8.4	37.0	36.3	39.7	31.0
APIs	7.8	0.9	3.1	14.5	1.6	11.2	11.6	(1.5)	(14.9)	0.4	(1.3)	4.8	19.7
Betalactum	6.1	(5.0)	(0.8)	13.9	3.6	19.6	2.2	2.0	(17.4)	0.6	16.8	4.0	20.3
Non Betalactum	11.5	12.2	10.9	15.7	(2.2)	(2.3)	10.0	(8.1)	(9.8)	0.0	(15.3)	6.5	18.5
As % of sales													
Raw material	45.8	44.9	44.4	43.4	44.5	43.2	43.8	41.3	40.7	39.9	41.9	41.2	44.9
Staff cost	10.9	11.1	11.5	10.9	11.5	11.3	11.4	12.7	13.3	11.7	12.5	14.4	14.0
Other expenses	18.1	17.8	17.4	17.8	17.2	17.0	21.5	20.8	18.7	19.7	18.3	19.9	17.3
Tax Rate	25.8	28.0	25.8	27.2	25.6	27.0	27.4	18.1	27.0	26.5	26.5	18.8	20.2
Margins (%)													
Gross Margins	54.2	55.1	55.6	56.6	55.5	56.8	56.2	58.7	59.3	60.1	58.1	58.8	55.1
EBITDA Margins	22.0	23.2	23.5	23.5	23.6	24.6	22.9	21.2	22.9	25.2	23.7	19.9	18.3
PAT margins	14.4	14.4	15.0	14.9	15.4	15.7	14.4	15.2	14.2	17.6	13.6	13.4	12.0

Source: Company; MOSL

Valuation and view

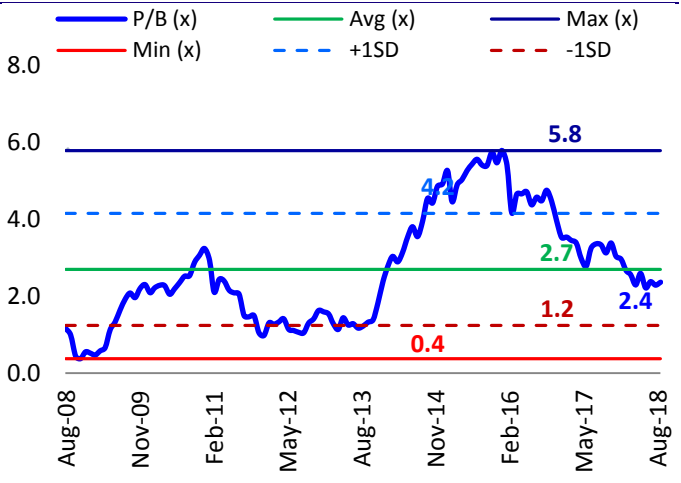
We cut our EPS estimates by 9%/7% to INR44.3 and INR49.5 to factor increased raw material prices. We roll our target to 15x 12M forward earnings and arrive at price target of INR750. We remain positive on ARBP on the back of strong ANDA pipeline, consistency in compliance and robust growth in EU business. Maintain Buy on the stock.

Exhibit 9: PE Band (x)



Source: Company, MOSL

Exhibit 10: PB Band



Source: Company, MOSL

Story in charts

Exhibit 11: Formulation led sales growth

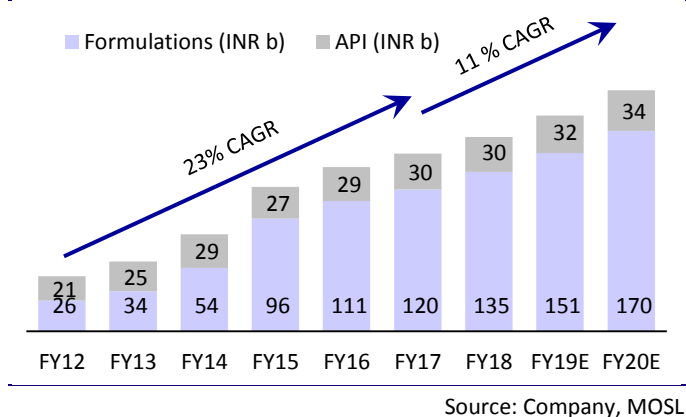


Exhibit 12: US Sales to grow at 11% CAGR over FY18-20E

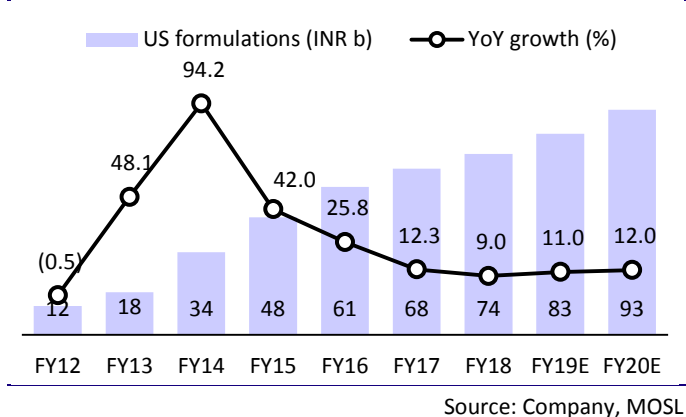


Exhibit 13: Margins to remain stable over FY18-20E

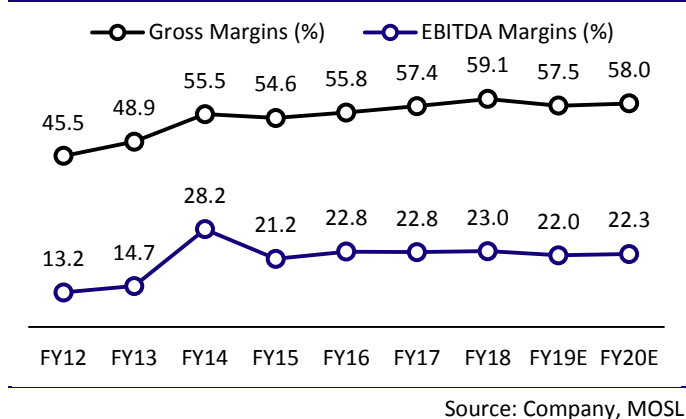


Exhibit 14: EBITDA to exhibit 10% CAGR from FY18-20E

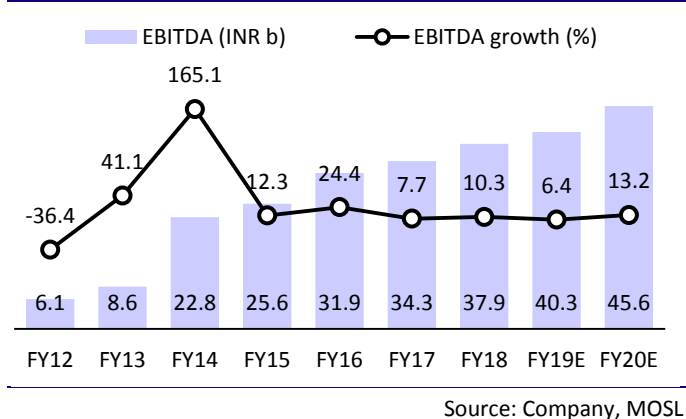


Exhibit 15: R&D expense to increase on rise to develop complex molecules

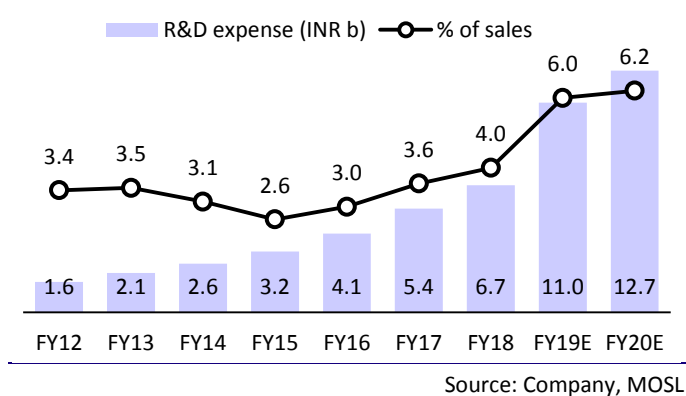
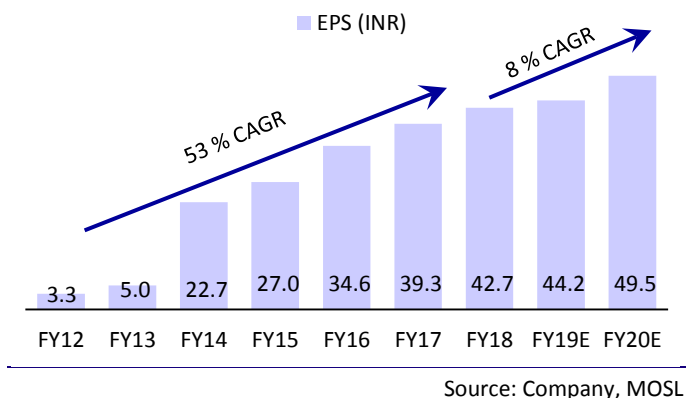


Exhibit 16: EPS growth to grow at ~8% CAGR from FY18-20E



Financials and Valuations

Consolidated - Income Statement

(INR Million)

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Total Income from Operations	80,998	121,205	139,553	150,897	164,998	183,259	204,611
Change (%)	38.3	49.6	15.1	8.1	9.3	11.1	11.7
Total Expenditure	58,170	95,569	107,671	116,556	127,113	142,942	158,983
% of Sales	71.8	78.8	77.2	77.2	77.0	78.0	77.7
EBITDA	22,828	25,636	31,882	34,341	37,885	40,317	45,628
Margin (%)	28.2	21.2	22.8	22.8	23.0	22.0	22.3
Depreciation	3,125	3,326	3,924	4,276	5,580	6,186	6,763
EBIT	19,703	22,310	27,958	30,065	32,305	34,131	38,865
Int. and Finance Charges	1,079	843	927	667	777	856	787
Other Income	232	808	701	538	1,020	800	500
PBT bef. EO Exp.	18,856	22,275	27,733	29,936	32,548	34,075	38,578
EO Items	-2,031	-596	-304	621	-168	-682	0
PBT after EO Exp.	16,825	21,679	27,429	30,557	32,380	33,393	38,578
Current Tax	3,635	5,966	7,207	7,596	8,183	8,178	9,644
Deferred Tax	0	0	0	0	0	0	0
Tax Rate (%)	21.6	27.5	26.3	24.9	25.3	24.5	25.0
Less: Mionrity Interest	-38	-45	-30	-55	-34	-55	-55
Reported PAT	13,228	15,758	20,252	23,015	24,231	25,270	28,988
Adjusted PAT	13,228	15,758	20,251	23,015	25,021	25,897	28,988
Change (%)	350.1	19.1	28.5	13.6	8.7	3.5	11.9
Margin (%)	16.3	13.0	14.5	15.3	15.2	14.1	14.2

Consolidated - Balance Sheet

(INR Million)

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Equity Share Capital	583	584	585	586	586	586	586
Total Reserves	36,919	50,975	72,288	93,133	116,218	140,023	167,547
Net Worth	37,502	51,559	72,873	93,719	116,804	140,609	168,133
Minority Interest	257	258	26	21	18	19	19
Deferred Liabilities	2,054	2,058	-1,823	-1,185	765	780	796
Total Loans	36,339	38,636	44,155	30,841	44,825	41,682	38,921
Capital Employed	76,151	92,511	115,230	123,397	162,413	183,090	207,868
Gross Block	41,066	53,821	41,312	53,650	70,719	80,719	90,719
Less: Accum. Deprn.	14,613	17,405	3,455	7,168	11,843	18,029	24,792
Net Fixed Assets	26,453	36,416	37,856	46,482	58,876	62,690	65,927
Goodwill on Consolidation	764	640	4,063	4,063	8,165	8,165	8,165
Capital WIP	3,097	4,196	8,359	12,374	13,995	13,995	13,995
Total Investments	198	198	1,230	2,459	3,115	3,115	3,115
Curr. Assets, Loans&Adv.	64,386	87,647	105,631	95,439	125,312	135,915	160,739
Inventory	23,675	36,113	40,561	43,305	58,584	53,346	58,861
Account Receivables	26,366	35,392	46,067	35,042	30,844	55,229	61,664
Cash and Bank Balance	1,786	4,691	8,003	5,135	12,616	16,341	29,215
Loans and Advances	12,559	11,451	11,001	11,957	23,268	11,000	11,000
Curr. Liability & Prov.	18,747	36,587	41,909	37,420	47,051	40,792	44,073
Account Payables	13,512	20,511	24,570	24,883	26,274	28,167	31,448
Other Current Liabilities	3,877	13,650	15,776	11,415	18,209	12,000	12,000
Provisions	1,358	2,426	1,563	1,123	2,568	625	625
Net Current Assets	45,640	51,060	63,722	58,019	78,260	95,124	116,666
Appl. of Funds	76,151	92,511	115,230	123,397	162,413	183,090	207,868

Financials and Valuations

Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Basic (INR)							
EPS	22.7	27.0	34.6	39.3	42.7	44.2	49.5
Cash EPS	28.1	32.7	41.3	46.6	52.2	54.8	61.0
BV/Share	64.3	88.3	124.5	160.0	199.4	240.0	287.0
DPS	1.5	2.3	2.0	2.5	2.5	2.5	2.5
Payout (%)	6.6	8.3	5.8	6.4	6.0	5.8	5.1
Valuation (x)							
P/E			17.6	15.5	14.3	13.8	12.3
Cash P/E			14.8	13.1	11.7	11.1	10.0
P/BV			4.9	3.8	3.1	2.5	2.1
EV/Sales			3.1	2.8	2.6	2.3	2.0
EV/EBITDA			13.4	12.1	11.2	10.3	8.8
Dividend Yield (%)			0.3	0.4	0.4	0.4	0.4
FCF per share			-0.5	27.0	-12.3	15.6	30.4
Return Ratios (%)							
RoE	41.6	35.4	32.5	27.6	23.8	20.1	18.8
RoCE	23.3	20.4	20.4	19.0	17.4	15.3	15.2
RoIC	24.2	20.9	22.8	22.5	20.4	18.3	18.7
Working Capital Ratios							
Asset Turnover (x)	1.1	1.3	1.2	1.2	1.0	1.0	1.0
Inventory (Days)	107	109	106	105	130	106	105
Debtor (Days)	116	105	120	85	68	110	110
Creditor (Days)	137	136	146	141	142	132	134
Working Cap. Turnover (Days)	198	140	146	128	145	157	156
Leverage Ratio (x)							
Current Ratio	3.4	2.4	2.5	2.6	2.7	3.3	3.6
Interest Cover Ratio	18	26	30	45	42	40	49
Debt/Equity	1.0	0.7	0.6	0.3	0.4	0.3	0.2

Consolidated - Cash Flow Statement

(INR Million)

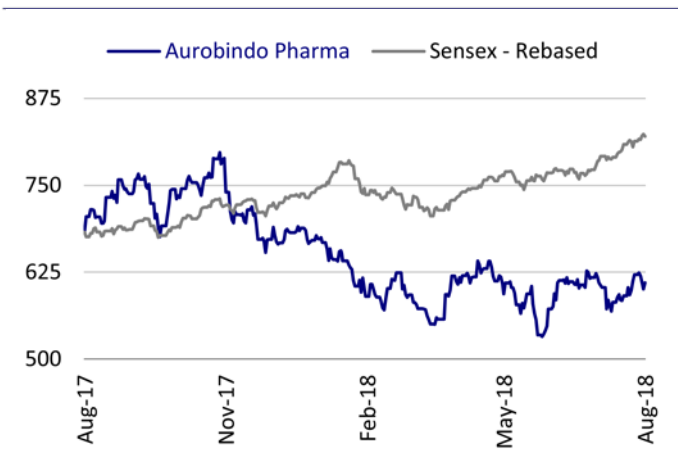
Y/E March	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
OP/(Loss) before Tax	19,703	22,310	27,443	30,608	32,305	34,131	38,865
Depreciation	3,125	3,326	3,924	4,276	5,580	6,186	6,763
Interest / Dividend recieved	232	808	689	384	1,020	800	500
Direct Taxes Paid	-3,635	-5,966	-7,326	-7,737	-8,183	-8,178	-9,644
(Inc)/Dec in WC	-13,533	-2,515	-10,794	6,110	-12,760	-13,139	-8,668
CF from Operations	5,893	17,963	13,936	33,641	17,962	19,800	27,816
Others	-2,031	-596	262	-856	-168	-682	0
CF from Operating incl EO	3,863	17,367	14,198	32,786	17,795	19,118	27,816
(inc)/dec in FA	-4,656	-14,389	-14,475	-16,942	-25,011	-10,000	-10,000
Free Cash Flow	-793	2,978	-277	15,844	-7,217	9,118	17,816
(Pur)/Sale of Investments	-25	0	23	-929	657	0	0
CF from Investments	-4,681	-14,388	-14,452	-17,870	-24,355	-10,000	-10,000
Issue of Shares	-910	-386	72	67	318	0	0
(Inc)/Dec in Debt	2,131	2,298	6,033	-17,279	13,982	-3,143	-2,761
Interest Paid	-1,079	-843	-835	-568	-777	-856	-787
Dividend Paid	-875	-1,314	-1,616	-1,372	-1,465	-1,465	-1,465
Others	1,253	172	-88	1,369	1,983	70	71
CF from Fin. Activity	520	-73	3,566	-17,784	14,042	-5,394	-4,942
Inc/Dec of Cash	-298	2,905	3,312	-2,868	7,482	3,724	12,874
Opening Balance	2,085	1,786	4,691	8,003	5,135	12,616	16,341
Closing Balance	1,786	4,691	8,003	5,134	12,616	16,341	29,215

Corporate profile

Company description

A well-integrated pharma company, Aurobindo Pharma (ARBP) features among the top 10 companies in India in terms of consolidated revenues. ARBP exports to over 125 countries across the globe with more than 70% of its revenues derived out of international operations. With multiple facilities approved by leading regulatory agencies such as USFDA, EU GMP, UK MHRA, South Africa-MCC, Health Canada and Brazil ANVISA, ARBP makes use of in-house R&D for rapid filing of patents, Drug Master Files (DMFs), Abbreviated New Drug Applications (ANDAs) and formulation dossiers across the world. ARBP is among the largest filers of DMFs and ANDAs from India.

Exhibit 1: Sensex rebased



Source: MOSL/Bloomberg

Exhibit 2: Shareholding pattern (%)

	Jun-18	Mar-18	Jun-17
Promoter	51.9	51.9	51.9
DII	15.8	15.6	14.2
FII	17.8	18.0	19.6
Others	14.5	14.5	14.3

Note: FII Includes depository receipts

Source: Capitaline

Exhibit 3: Top holders

Holder Name	% Holding
Hdfc Trustee Company Limited-Hdfc Equity Fund	6.0
Aditya Birla Sun Life Trustee Private Limited A/C Aditya Birla Sun Life Focused Equity Fund - Series	2.8
Reliance Capital Trustee Co. Ltd-A/C Reliance Equity Savings Fund	2.3
Amansa Holdings Private Limited	1.2
Hdfc Trustee Company Limited-Hdfc Equity Fund	6.0

Source: Capitaline

Exhibit 4: Top management

Name	Designation
K Ragunathan	Chairman
K Nithyananda Reddy	Vice Chairman & Whole Time Dir
N Govindarajan	Managing Director
B Adi Reddy	Company Secretary

Source: Capitaline

Exhibit 5: Directors

Name	Name
P V Ramprasad Reddy	Avnit Bimal Singh
D Rajagopala Reddy	M Sitarama Murthy
M Madan Mohan Reddy	M Sivakumaran
P Sarath Chandra Reddy	

*Independent

Exhibit 6: Auditors

Name	Type
B S R & Associates LLP	Statutory
D V Rao & Associates	Secretarial Audit
S R Batliboi & Associates LLP	Statutory

Source: Capitaline

Exhibit 7: MOSL forecast v/s consensus

EPS (INR)	MOSL forecast	Consensus forecast	Variation (%)
FY17	40.5	42.0	-3.5
FY18	48.1	49.4	-2.6
FY19	57.2	55.0	4.0

Source: Bloomberg

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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