

Aurobindo Pharma

BUY

INDUSTRY PHARMA

CMP (as on 10 Aug 2018) **Rs 610**
Target Price **Rs 691**

Nifty 11,430

Sensex 37,869

KEY STOCK DATA

Bloomberg ARBP IN

No. of Shares (mn) 586

MCap (Rs bn) / (\$ mn) 357/5,190

6m avg traded value (Rs mn) 1,512

STOCK PERFORMANCE (%)

52 Week high / low **Rs 809/527**

3M 6M 12M

Absolute (%) 2.7 3.5 (11.0)

Relative (%) (4.8) (7.9) (31.1)

SHAREHOLDING PATTERN (%)

Promoters 51.9

FIs & Local MFs 15.8

FPIs 17.8

Public & Others 14.5

Source : BSE

Resilient performance

Aurobindo Pharma's (ARBP) revenue in 1QFY19 came in at Rs 4.6bn, up 16.7%YoY and 5%QoQ, beating our estimates by 8%. This was aided by good double-digit growth in the formulations segment, with US and Europe/RoW growing at 11.5% and 31% YoY respectively. Gross margin dropped to 55% (v/s 59% in 1QFY18) due to one-off inventory provisions and shelf stock adjustment. EBITDA stood at Rs 7.8bn (down 7%YoY) and margin was at 18.4% (down 477bps YoY/152bps QoQ). PAT at Rs 4.6bn was also down 12.1%YoY impacted by forex loss of Rs 682mn.

Despite unfavourable business environment in the US when peers have seen precipitous fall in their revenues and profitability over last two years, ARBP's portfolio has been resilient and maintained the growth momentum. With near term opportunities like Toprol XL, Prevacid ODT, and Welchol, and several injectable products, we believe ARBP can continue to grow at 8% in top-line while earnings growth will be at 15% CAGR over FY18-20E. At CMP, the stock is trading at 16.4x FY19E and 13.2x

Financial Summary

Year Ending March (Rs mn)	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)	FY17	FY18	FY19E	FY20E
Net Sales	42,503	36,420	16.7	40,491	5.0	149,295	164,998	172,736	191,612
EBITDA	7,792	8,416	(7.4)	8,040	(3.1)	34,343	37,885	34,374	41,580
APAT	4,557	5,185	(12.1)	5,286	(13.8)	23,017	20,138	21,457	26,590
Diluted EPS (Rs)	7.8	8.9	(12.1)	9.0	(13.8)	39.3	34.4	36.6	45.4
P/E (x)						15.3	17.5	16.4	13.2
RoE (%)						27.6	19.1	16.9	17.8

Source: Company, HDFC sec Inst Research # Consolidated

FY20E, at a sharp discount to peers. **Maintain BUY rating, with a revised TP of Rs 691 (16x FY20E).**

Highlights of the quarter

- **The US business:** ARBP filed for 7 ANDAs, received final approval for 13, and launched 14 products in 1QFY19. It is guiding for 10+ more derma filings over 12 months and 40+ onco/hormone filings by CY19. The US business volume grew by low double digits, and ~30% of the sales came from new business opportunities. Anticipates 30% growth in injectable portfolio while OTC portfolio could reach US\$ 60mn in revenues.
- **Concall takeaways:** (1) ARV segment will perform better in 2Q. (2) Apotex business acquisition will enable entry into Poland and Czech, while also strengthening presence in other European countries. (3) Shelf stock adjustment of ~Rs900mn reduced gross margin. (4) Working capital increased by ~US\$ 63mn, with net debt increased by US\$ 33mn. (5) Finance cost was ~2.3% for 1Q, expected to go up to 2.9% by 3Q.
- **Near-term outlook:** Important product launches in the US would be the only near-term trigger for the stock.

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Revenue growth was driven by uptick in Europe and ROW which grew 31%YoY in 1QFY19

EBITDA margin at 18.3% was ~230bps below our estimates, largely due to the impact of shelf stock adjustment

Forex loss led to further erosion of profits

Quarterly Financials Snapshot (Consolidated)

Particulars	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)
Net Sales	42,503	36,420	16.7	40,491	5.0
Material Expenses	19,073	14,978	27.3	16,695	14.2
Employee Expenses	5,961	4,902	21.6	5,813	2.6
Other Expenses	9,677	8,124	19.1	9,943	(2.7)
EBITDA	7,792	8,416	(7.4)	8,040	(3.1)
Depreciation	1,545	1,312		1,566	
EBIT	6,247	7,104	(12.1)	6,474	(3.5)
Other Income	437	221		438	
Interest Cost	295	169		247	
FX Gains / (Loss)	(682)	(77)		(159)	
PBT	5,707	7,080	(19.4)	6,506	(12.3)
Tax	1,155	1,910		1,223	
Minority Interest	5	15		3	
RPAT	4,557	5,185	(12.1)	5,286	(13.8)
EO Items (Adj For Tax)	-	-		-	
APAT	4,557	5,185	(12.1)	5,286	(13.8)

Source: Company, HDFC sec Inst Research

Margin Analysis

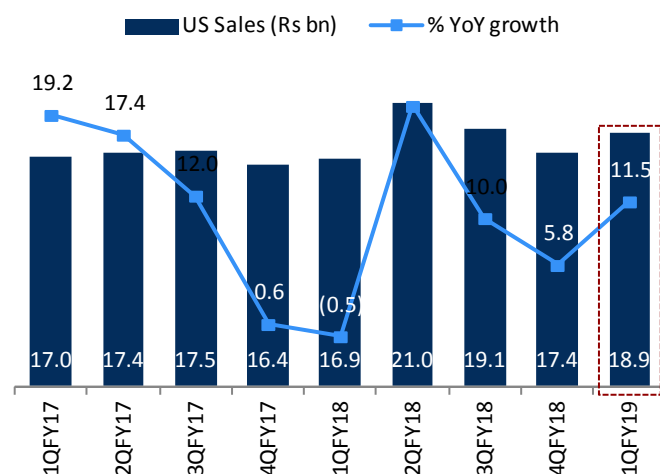
	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)
Material Expenses % Net Sales	44.9	41.1	375	41.2	364
Employee Expenses % Net Sales	14.0	13.5	57	14.4	(33)
Other Expenses % Net Sales	22.8	22.3	46	24.6	(179)
EBITDA Margin (%)	18.3	23.1	(477)	19.9	(152)
Tax Rate (%)	20.2	27.0	(673)	18.8	144
APAT Margin (%)	10.7	14.2	(352)	13.1	(233)

Source: Company, HDFC sec Inst Research

Text Box: US segment showed good growth in revenue which is expected to further grow in subsequent quarters on the back of growth in injectables and new product launches

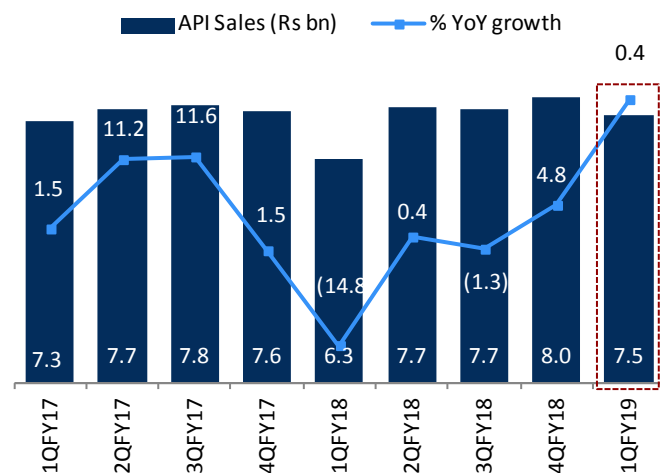
Gross and EBITDA margins declined YoY, expecting boost by improvement in business mix and increasing contribution of injectable sales

US Formulations: In-Line With Estimates



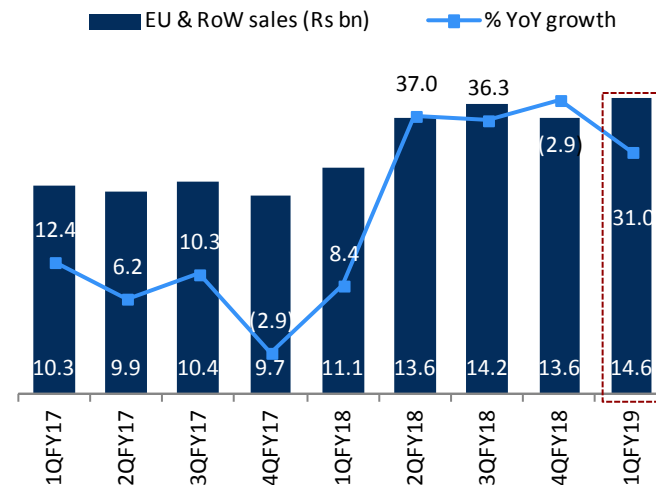
Source: Company, HDFC sec Inst Research

API Revenues: Decline In ARV APIs



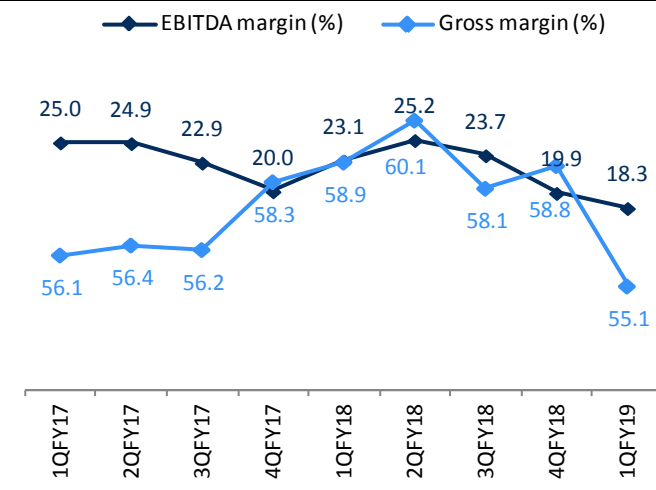
Source: Company, HDFC sec Inst Research

EU Sales Boosted By New Product Launches And Generis Integration



Source: Company, HDFC sec Inst Research

EBITDA Margin Expansion To Be Limited Hereon



Source: Company, HDFC sec Inst Research

ARV segment expected to perform better in 2Q aided by DTG contracts

Apotex business acquisition will boost Europe revenue in 2HFY19

Segmental Quarterly Performance

(Rs mn)	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)
US	18,896	16,949	11.5	17,388	8.7
Europe &RoW	14,556	11,115	31.0	13,612	6.9
ARVs	1,556	2,446	(36.4)	1,486	4.7
Formulation (sub-total)	35,008	30,510	14.7	32,486	7.8
APIs (sub-total)	7,495	6,251	19.9	7,996	(6.3)
Total	42,503	36,761	15.6	40,482	5.0

Source: HDFC sec Inst Research

Assumptions

	FY16	FY17	FY18	FY19E	FY20E
US	60,786	68,272	74,421	77,399	86,682
<i>Growth (%)</i>	<i>30.1</i>	<i>12.3</i>	<i>9.0</i>	<i>4.0</i>	<i>12.0</i>
Europe	31,304	32,771	43,544	47,028	51,730
<i>Growth (%)</i>	<i>(2.0)</i>	<i>4.7</i>	<i>32.9</i>	<i>8.0</i>	<i>10.0</i>
ARV	12,093	11,854	8,396	8,396	9,236
<i>Growth (%)</i>	<i>25.5</i>	<i>(2.0)</i>	<i>(29.2)</i>	<i>-</i>	<i>10.0</i>
RoW	6,461	7,556	8,971	10,182	11,557
<i>Growth (%)</i>	<i>13.7</i>	<i>16.9</i>	<i>18.7</i>	<i>13.5</i>	<i>13.5</i>
SSPs - API	8,708	9,886	8,897	9,342	9,809
<i>Growth (%)</i>	<i>0.8</i>	<i>13.5</i>	<i>(10.0)</i>	<i>5.0</i>	<i>5.0</i>
Ceph - API	9,858	10,548	11,026	11,687	12,388
<i>Growth (%)</i>	<i>6.0</i>	<i>7.0</i>	<i>6.0</i>	<i>6.0</i>	<i>6.0</i>
ARVs - API	10,270	9,986	9,699	10,669	12,269
<i>Growth (%)</i>	<i>12.6</i>	<i>(2.8)</i>	<i>(2.9)</i>	<i>10.0</i>	<i>15.0</i>
Total	139,480	150,873	164,954	174,703	193,672
<i>Growth (%)</i>	<i>13.7</i>	<i>8.2</i>	<i>9.3</i>	<i>5.9</i>	<i>10.9</i>

Source: HDFC sec Inst Research

Peer Set Comparison

	Mcap (Rs bn)	CMP (Rs/sh)	Reco	TP/FV	Adj EPS (Rs/sh)				P/E (x)				RoE (%)			
					FY17	FY18	FY19E	FY20E	FY17	FY18	FY19E	FY20E	FY17	FY18	FY19E	FY20E
Sun Pharma	1,333	554	BUY	640	26.0	13.0	16.4	24.6	21.3	42.7	33.7	22.5	17.9	9.1	12.3	14.8
Cipla	499	621	NEU	595	12.5	17.5	22.5	28.6	49.7	35.4	27.6	21.7	8.4	10.5	12.0	13.7
Cadila Healthcare	386	377	BUY	525	14.5	12.9	14.6	21.2	25.9	29.3	25.7	17.8	23.5	16.8	16.1	20.1
Dr Reddy's Labs	376	2,214	NEU	2,340	72.7	59.2	75.7	102.5	30.5	37.4	29.2	21.6	9.5	7.8	9.5	11.5
Lupin	364	809	BUY	1,000	33.4	38.0	27.4	45.3	24.3	21.3	29.5	17.9	12.2	12.7	8.9	13.5
Aurobindo Pharma	352	610	BUY	691	39.3	34.4	36.6	45.4	15.3	17.5	16.4	13.2	27.6	19.1	16.9	17.8
Divi's Labs	298	1,124	NEU	1,150	39.9	33.0	44.6	51.4	28.1	34.0	25.2	21.9	22.0	15.5	18.7	18.9
Torrent Pharma	287	1,697	NEU	1,540	51.2	40.1	46.1	69.9	33.1	42.4	36.8	24.3	22.1	15.1	15.9	20.9
Alkem Laboratories	246	2,060	BUY	2,445	74.6	57.6	76.8	101.9	27.6	35.8	26.8	20.2	21.9	14.8	17.6	20.1
Glenmark	167	591	BUY	710	29.6	17.5	27.0	38.8	20.0	33.8	21.9	15.2	18.1	9.4	12.8	16.1
Jubilant Life Sciences	114	731	BUY	990	37.0	46.6	57.9	70.1	19.8	15.7	12.6	10.4	18.0	19.3	20.1	20.3
Alembic Pharma	109	578	NEU	560	21.4	21.9	23.8	31.1	27.0	26.4	24.2	18.6	23.0	20.0	18.8	20.9
Laurus Labs	46	438	NR	505	18.0	15.8	18.3	28.2	24.3	27.6	24.0	15.5	17.4	11.9	12.3	16.6
Dishman Carbogen Amcis	42	259	BUY	440	9.0	9.6	13.4	19.9	28.8	27.1	19.3	13.1	3.0	3.1	4.2	5.9
Strides Shasun	37	411	BUY	480	34.0	12.7	15.5	28.7	12.1	32.4	26.5	14.3	13.1	4.4	5.5	9.6
Suven Life Sciences	30	235	NR	450	6.8	9.7	10.3	11.4	34.3	24.2	22.7	20.6	13.8	17.2	16.0	15.5
Granules India	26	104	BUY	120	7.5	5.2	7.8	10.0	13.9	19.9	13.4	10.5	21.0	12.0	14.3	16.5
Neuland Labs	6	687	BUY	1,000	42.6	11.0	28.9	62.3	16.1	62.7	23.8	11.0	12.8	2.2	5.5	11.1

Source: HDFC sec Inst Research

Change In Estimates (Consolidated)

Rs mn	Previous			New			% Chg		
	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E
Net Sales	164,998	173,575	192,535	164,998	172,736	191,612	0.0	(0.5)	(0.5)
EBITDA	37,885	37,145	44,091	37,885	34,374	41,580	0.0	(7.5)	(5.7)
APAT	20,138	22,875	28,124	20,138	21,457	26,590	0.0	(6.2)	(5.5)

Source: HDFC sec Inst Research

Income Statement (Consolidated)

Year ending March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Net Revenues	138,072	149,295	164,998	172,736	191,612
Growth (%)	13.9	8.1	10.5	4.7	10.9
Material Expenses	61,621	64,343	67,527	75,140	80,477
Employee Expenses	15,426	17,678	21,308	23,319	24,910
SG&A Expenses	9,838	11,190	12,638	11,746	12,455
Other Expenses	19,306	21,742	25,640	28,156	32,191
EBITDA	31,881	34,343	37,885	34,374	41,580
EBITDA Margin (%)	23.1	23.0	23.0	19.9	21.7
EBITDA Growth (%)	24.4	7.7	10.3	(9.3)	21.0
Depreciation	3,924	4,276	5,580	6,198	6,560
EBIT	27,957	30,067	32,306	28,177	35,019
Other Income (Incl EO Items)	701	538	1,020	1,050	850
Interest	927	667	777	1,066	955
PBT	27,732	29,938	32,548	28,160	34,914
Tax (Incl Deferred)	7,207	7,596	8,183	6,758	8,379
RPAT	20,524	22,341	24,365	21,402	26,535
Minority Interest	(30)	(55)	29	(55)	(55)
EO (Loss) / Profit (Net Of Tax)	304	(621)	4,199	-	-
APAT	20,250	23,017	20,138	21,457	26,590
APAT Growth (%)	28.5	13.7	(12.5)	6.6	23.9
Adjusted EPS (Rs)	34.6	39.3	34.4	36.6	45.4

Source: Company, HDFC sec Inst Research

Balance Sheet (Consolidated)

Year ending March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
SOURCES OF FUNDS					
Share Capital - Equity	585	586	586	586	586
Reserves	72,288	93,133	116,218	136,210	161,336
Total Shareholders Funds	72,873	93,719	116,804	136,796	161,921
Minority Interest	26	21	18	19	19
Long Term Debt	7,428	1,814	4,512	3,384	2,538
Short Term Debt	36,727	29,027	40,313	37,088	33,379
Total Debt	44,155	30,841	44,825	40,472	35,917
Net Deferred Taxes	(1,823)	(1,185)	765	780	796
Other Non-Current Liabilities & Provns	234	224	450	550	550
TOTAL SOURCES OF FUNDS	115,464	123,621	162,863	178,617	199,204
APPLICATION OF FUNDS					
Net Block	37,734	44,275	58,876	62,678	66,118
CWIP	9,663	15,596	13,995	8,500	6,500
Goodwill	4,063	4,063	8,165	8,165	8,165
Investments	1,229	2,459	3,115	3,115	3,115
Other Non-current Assets	1,506	2,363	2,056	3,425	3,425
Total Non-current Assets	54,196	68,755	86,209	85,884	87,323
Cash & Equivalents	8,003	12,524	12,616	34,896	47,501
Inventories	40,561	43,305	58,584	47,348	50,712
Debtors	46,067	27,653	30,844	49,691	55,121
Other Current Assets	8,313	8,580	21,211	2,825	2,825
Total Current Assets	94,941	79,538	110,639	99,865	108,658
Creditors	24,570	24,883	26,274	28,527	30,779
Other Current Liabilities & Provns	17,105	12,313	20,327	13,500	13,500
Total Current Liabilities	41,675	37,196	46,601	42,027	44,279
Net Current Assets	53,265	42,342	64,038	57,837	64,379
TOTAL APPLICATION OF FUNDS	115,464	123,621	162,863	178,617	199,204

Source: Company, HDFC sec Inst Research

Cash Flow

Year ending March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Reported PBT	27,030	29,399	31,528	27,110	34,064
Non-operating & EO items	428	423	1,978	(40)	(39)
Interest expenses	927	667	777	1,066	955
Depreciation	3,924	4,276	5,580	6,198	6,560
Working Capital Change	(9,949)	10,224	(20,148)	4,932	(6,542)
Tax Paid	(6,727)	(6,958)	(6,233)	(6,743)	(8,364)
OPERATING CASH FLOW (a)	15,633	38,032	13,482	32,523	26,635
Capex	(14,962)	(16,756)	(23,698)	(4,505)	(8,000)
<i>Free cash flow (FCF)</i>	<i>671</i>	<i>21,276</i>	<i>(10,216)</i>	<i>28,019</i>	<i>18,635</i>
Investments	(2,077)	(521)	134	95	95
Non-operating Income	701	538	1,020	1,050	850
INVESTING CASH FLOW (b)	(16,337)	(16,739)	(22,544)	(3,360)	(7,055)
Debt Issuance/(Repaid)	6,073	(13,314)	13,984	(4,353)	(4,555)
Interest Expenses	(927)	(667)	(777)	(1,066)	(955)
<i>FCFE</i>	<i>4,443</i>	<i>7,312</i>	<i>4,145</i>	<i>23,744</i>	<i>14,070</i>
Share Capital Issuance	293	1	-	-	-
Dividend	(1,170)	(1,465)	(1,465)	(1,465)	(1,465)
Others	(54)	(1,327)	548	0	-
FINANCING CASH FLOW (c)	4,215	(16,772)	12,291	(6,884)	(6,974)
NET CASH FLOW (a+b+c)	3,512	4,521	3,228	22,280	12,605
EO Items, Others	-	-	-	-	-
Closing Cash & Equivalents	8,002	12,524	15,752	34,896	47,501

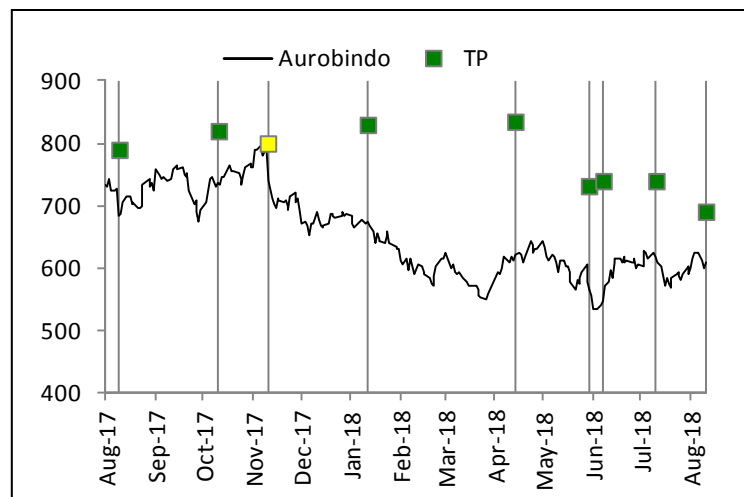
Source: Company, HDFC sec Inst Research

Key Ratios

	FY16	FY17	FY18	FY19E	FY20E
PROFITABILITY (%)					
GPM	55.4	56.9	59.1	56.5	58.0
EBITDA Margin	23.1	23.0	23.0	19.9	21.7
APAT Margin	14.7	15.4	12.2	12.4	13.9
RoE	32.0	27.6	19.1	16.9	17.8
RoIC (or Core RoCE)	21.8	21.3	19.2	15.2	18.9
RoCE	20.4	19.7	14.5	13.0	14.5
EFFICIENCY					
Tax Rate (%)	26.0	25.4	25.1	24.0	24.0
Fixed Asset Turnover (x)	3.3	2.9	2.3	2.1	2.1
<i>Inventory (days)</i>	<i>107.2</i>	<i>105.9</i>	<i>129.6</i>	<i>100.1</i>	<i>96.6</i>
<i>Debtors (days)</i>	<i>121.8</i>	<i>67.6</i>	<i>68.2</i>	<i>105.0</i>	<i>105.0</i>
<i>Other Current Assets (days)</i>	<i>22.0</i>	<i>21.0</i>	<i>46.9</i>	<i>6.0</i>	<i>5.4</i>
<i>Payables (days)</i>	<i>65.0</i>	<i>60.8</i>	<i>58.1</i>	<i>60.3</i>	<i>58.6</i>
<i>Other Current Liab & Provns (days)</i>	<i>45.2</i>	<i>30.1</i>	<i>45.0</i>	<i>28.5</i>	<i>25.7</i>
<i>Cash Conversion Cycle (days)</i>	<i>140.8</i>	<i>103.5</i>	<i>141.7</i>	<i>122.2</i>	<i>122.6</i>
Debt/EBITDA (x)	1.4	0.9	1.2	1.2	0.9
Net D/E (x)	0.5	0.2	0.3	0.0	(0.1)
Interest Coverage (x)	30.1	45.1	41.6	26.4	36.7
PER SHARE DATA (Rs)					
EPS	34.6	39.3	34.4	36.6	45.4
Dividend	2.0	2.5	2.5	2.5	2.5
Book Value	124.5	160.0	199.4	233.5	276.4
VALUATION					
P/E (x)	17.4	15.3	17.5	16.4	13.2
P/BV (x)	4.8	3.8	3.0	2.6	2.2
EV/EBITDA (x)	12.2	10.8	10.1	10.4	8.2
EV/Revenues (x)	2.8	2.5	2.3	2.1	1.8
OCF/EV (%)	4.0	10.3	3.5	9.1	7.8
FCF/EV (%)	0.2	5.7	(2.7)	7.8	5.5
FCFE/Mkt Cap (%)	1.3	2.1	1.2	6.7	4.0
Dividend Yield (%)	0.3	0.4	0.4	0.4	0.4

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
10-Aug-17	684	BUY	790
10-Oct-17	729	BUY	820
11-Nov-17	740	NEU	800
11-Jan-18	675	BUY	830
13-Apr-18	610	BUY	835
29-May-18	579	BUY	732
13-Jun-18	596	BUY	740
10-Jul-18	623	BUY	740
11-Aug-18	610	BUY	691

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

Disclosure:

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