

Granules India

BSE SENSEX	S&P CNX
35,591	10,652
Bloomberg	GRAN IN
Equity Shares (m)	229
M.Cap.(INRb)/(USDb)	23.5 / 0.3
52-Week Range (INR)	135 / 72
1, 6, 12 Rel. Per (%)	4/-8/-29
12M Avg Val (INR M)	330
Free float (%)	55.1

CMP: INR92 TP: INR140 (+52%) Buy

Superior performance persists; outlook remains robust


- GRAN delivers record quarterly EBITDA:** GRAN's 3QFY19 sales came in at INR6.3b (v/s our estimate of INR5.5b), up ~54% YoY, led by API and formulation (FD) segment. Gross margin (GM) declined by ~600bp YoY (+200bp QoQ) to 43.2%, primarily due to increased competition and higher input costs. Despite sharp contraction in GM, GRAN was able to maintain EBITDA margin at 17.8% (flat YoY; +60bp QoQ) due to better operating leverage. Absolute EBITDA increased by ~53% YoY to INR1.1b (v/s our estimate of INR970m) on back of strong revenue growth. For 9MFY19, profit from JV/associates stood at INR297m v/s INR127m YoY. PAT grew at a higher rate than EBITDA due to higher other income and lower tax rate of 31% (v/s 36% in 3QFY18). PAT stood at INR603m (+72% YoY). For 9MFY19, sales/EBITDA/PAT stood at INR16.7b (+40% YoY)/INR2.9b (+26% YoY)/INR1.7b (+54% YoY).
- FD/API led growth in revenue:** Fixed dosage (FD) (49% of sales) grew by ~88% YoY to INR3.1b and API (34% of sales) grew 45% YoY to INR2.1b. Limited competition in FD and improved realizations in PFI/API are the key factors for YoY revenue growth in the quarter. Geography-wise, revenue from North America grew 122%/71% for 3QFY19/9MFY19 and forms 52% of sales.
- Other key highlights:** (1) GRAN has guided for four ANDA approvals in the next 3-6 months; (2) contribution from JV was subdued due to annual maintenance shutdown; it's expected to be on-track from 4QFY19; (3) strong growth in FD was due to Methocarbamol and Ibuprofen, which were launched by GRAN under its own label; and (4) working capital cycle is down to 124 days from 137 days end-FY18.
- Valuation and view:** We raise FY19/FY20 EPS by 16%/10% to INR8.9/INR10.4 to factor in strong 3Q, superior performance in formulation and improved capacity utilization. We reduce P/E multiple to 13x (from earlier 15x) to factor in the current headwinds in the US generics market. We maintain our price target at INR140 on 12M forward earnings basis. Maintain **Buy**.

Financials & Valuations (INR b)

Y/E Mar	2019E	2020E	2021E
Net Sales	22.8	26.1	30.5
EBITDA	3.9	4.9	5.8
PAT	2.3	2.6	3.1
EPS (INR)	8.9	10.4	12.3
Gr. (%)	70.2	16.5	18.4
BV/Sh (INR)	57.6	64.0	72.4
RoE (%)	16.3	17.0	18.0
RoCE (%)	13.2	14.9	16.6
P/E (x)	10.4	8.9	7.5
P/BV (x)	1.6	1.4	1.3

Estimate change 

TP change 

Rating change 

Quarterly Performance

Y/E March (Consolidated)	FY18				FY19E				FY18	FY19E	(INR Million)	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE			Est. 3QE	Var. vs Est
Net Sales	3,860	3,926	4,107	5,038	4,532	5,809	6,318	6,168	16,918	22,827	5,545	13.9%
YoY Change (%)	10.3	7.9	14.3	38.7	17.4	48.0	53.8	22.4	17.9	34.9	35.0	
EBITDA	842	769	740	436	726	1,005	1,133	1,062	2,784	3,926	970	16.8%
Margins (%)	21.8	19.6	18.0	8.7	16.0	17.3	17.9	17.2	16.5	17.2	17.5	
Depreciation	176	186	196	204	245	265	270	312	762	1,093	285	
Interest	82	104	82	62	65	76	75	79	331	295	80	
Other Income	4	68	9	97	147	42	59	49	108	297	30	
PBT before EO expense	515	547	471	267	563	706	847	720	1,800	2,835	635	33.4%
Tax	177	193	169	95	191	234	265	190	634	879	222	
Rate (%)	34.4	35.2	35.9	35.6	34.0	33.1	31.2	26.4	35.2	31.0	35.0	
(Profit)/Loss of JV/Asso. Cos.	-30	-49	-49	-32	-146	-130	-21	-3	-160	-300	-70	
PAT (Ex associate income)	338	355	302	172	372	472	582	530	1,166	1,956	413	41.1%
Reported PAT	368	403	350	204	518	603	603	533	1,326	2,256	483	24.9%
YoY Change (%)	-5.5	-1.2	-10.1	-55.3	40.7	49.4	72.3	160.5	-19.4	70.2	37.9	
Margins (%)	9.5	10.3	8.5	4.1	11.4	10.4	9.5	8.6	7.8	9.9	8.7	

E: MOSL Estimates

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Key con-call takeaways

- GRAN has guided for ~20% CAGR in sales and ~25% CAGR in earnings over the next three years. Company plans to achieve this on back of:
 - Scale-up in the US business
 - Commercialization of key APIs in the Oncology segment
 - Optimum capacity utilization
- Prices of key raw materials from China have started to moderate. GRAN expects prices to decline further 4Q onwards, thereby improving gross margins, going forward.
- During the quarter, contribution from JV was lower due to shutdown of the JV facility on account of annual routine maintenance.
- Cash flow from operation (CFO) was INR1b for the quarter. On an annualized basis, CFO is expected to be ~INR5b for FY19 and ~INR6-7b in 2-3 years' time. This will be largely used for re-payment of debt.
- Net debt stood at INR9.4b v/s INR10b in 2QFY19.
- GRAN has guided for INR1.4b capex in FY20 and INR400-500m (annualized) thereafter for maintenance capex. Granules Pharmaceutical Inc. (GPI) would spend ~USD10m for capacity addition.
- GRAN has ~30% market share in the US for Ibuprofen. Sales during the quarter were driven by higher prices and increase in market share. Its competitor is expected to resume production from April 2019, gradually ramping up its capacity.
- Working capital cycle is down to 124 days from 137 days end-FY18.
- R&D spends for the quarter was at INR320m, of which INR140m was charged to P&L and balance was capitalized. For 9MFY19, INR410m was charged to P&L and INR440m capitalized.
- Company has maintained its guidance of 10-12 ANDA filings for FY19. It expects four ANDA approvals in the next 3-6 months.
- Omnicem and Biocause sales, EBITDA margin and PAT margin for first three quarters stood at:

Exhibit 1: Omnicem

(INR m)	1QFY19	2QFY19	3QFY19
Sales	970	170	120
EBITDA	194	-14	-18
PAT	155	-53	-58

Source: Company, MOSL

Exhibit 2: Biocause JV

(INR m)	2QFY19	3QFY19
Sales	1090	630
EBITDA	382	126
PAT	316	101

Source: Company, MOSL

- GRAN expects Omnicem's 4QFY19 performance to come in line with 1QFY19. For Biocause, it expects 4QFY19 to be better than 2QFY19.
- Forex gain during the quarter was INR40m, which was included in other income.

Story in Charts

Exhibit 3: 54% YoY growth in revenue (3QFY19)

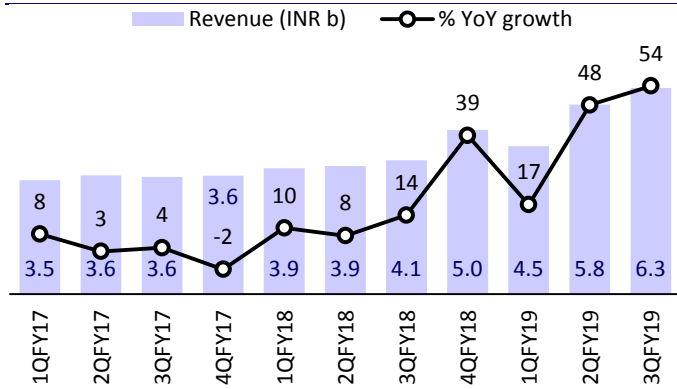


Exhibit 4: EBITDA margins remained flat YoY

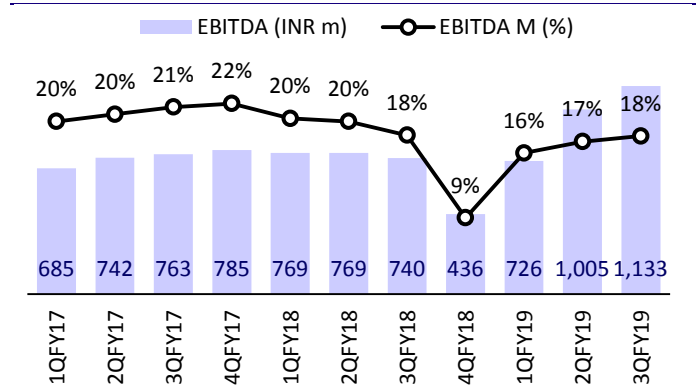


Exhibit 5: Revenues to exhibit 22% CAGR over FY18-21E

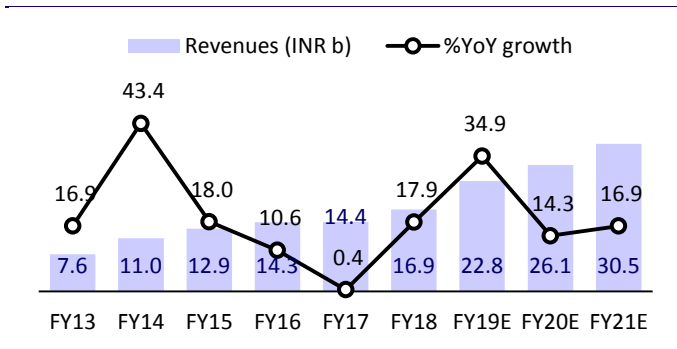


Exhibit 6: EBITDA margin to improve gradually

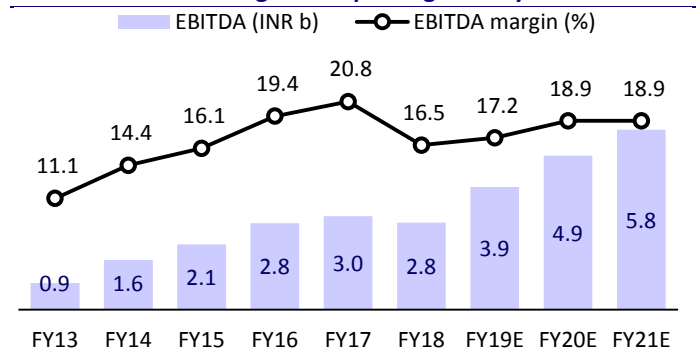


Exhibit 7: Formulation contribution to increase

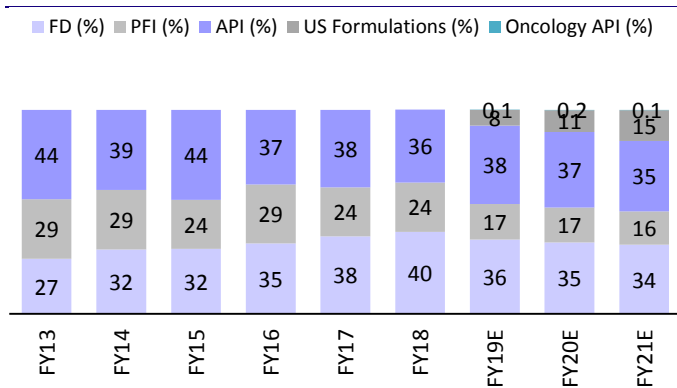


Exhibit 8: PAT to grow by ~33% CAGR from FY18-21E

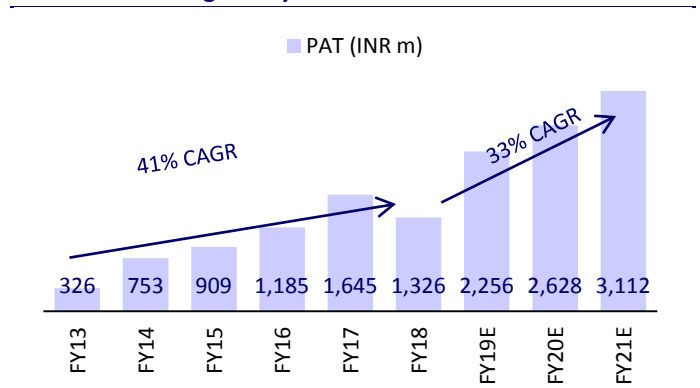
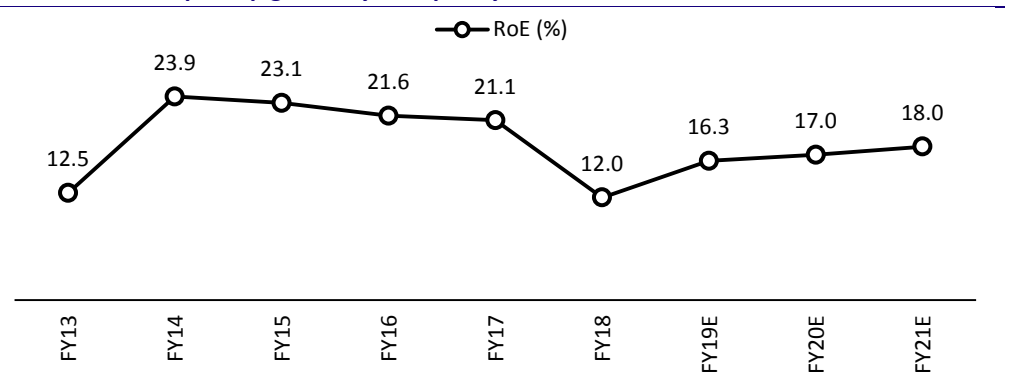


Exhibit 9: RoE to pick up gradually as capex cycle ends



Source: Company, MOSL

Valuation and view

Over FY13-18, GRAN reported 33% earnings CAGR on improved profitability, higher operating leverage and superior business mix. It expanded its finished dosages business at a CAGR of 27% over FY13-18, leading to higher profitability and improved utilization of its existing capacity of 18b tablets. Profitability of the PFI business has also improved substantially, with implementation of 6MT order capacity. As a result, GRAN expanded its EBITDA margins from 11.1% in FY13 to 16.5% in FY18.

We believe the capex cycle of GRAN is nearing completion and its efforts should start delivering from here on. Margins remain in recovery mode due to passing of the increased raw material cost to customers and increased share of formulation business to the US market. We expect 52% CAGR in earnings over FY18-21.

We raise FY19/FY20 EPS by 16%/10% to INR8.9/INR10.4 to factor in strong 3Q, superior performance in formulation and improved capacity utilization. We reduce P/E multiple to 13x (from 15x earlier) to factor in the current ongoing headwinds in the US generics market and maintain our price target at INR140 on 12M forward earnings basis. Maintain Buy.

Key catalysts to drive stock's performance over the medium term

- Finished dosages product approvals from regulated markets.
- Ramp-up of production from new capacity.
- Higher-than- expected realizations from Omnicem JV.

Risks to our investment thesis

- Pricing pressure on existing products.
- Regulatory risks related to already approved manufacturing facilities.

Financials and Valuations

Consolidated - Income Statement

(INR Million)

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E	FY21E
Total Income from Operations	10,959	12,929	14,295	14,353	16,918	22,827	26,099	30,507
Change (%)	43.4	18.0	10.6	0.4	17.9	34.9	14.3	16.9
Total Expenditure	9,376	10,843	11,528	11,364	14,134	18,901	21,166	24,741
% of Sales	85.6	83.9	80.6	79.2	83.5	82.8	81.1	81.1
EBITDA	1,583	2,086	2,767	2,988	2,784	3,926	4,933	5,766
Margin (%)	14.4	16.1	19.4	20.8	16.5	17.2	18.9	18.9
Depreciation	298	527	643	715	762	1,093	1,279	1,393
EBIT	1,285	1,560	2,124	2,273	2,022	2,833	3,654	4,373
Int. and Finance Charges	204	323	399	323	331	295	306	306
Other Income	43	43	77	99	108	297	157	183
PBT bef. EO Exp.	1,124	1,280	1,802	2,050	1,800	2,835	3,504	4,250
EO Items	0	0	0	0	0	0	0	0
PBT after EO Exp.	1,124	1,280	1,802	2,050	1,800	2,835	3,504	4,250
Current Tax	305	287	535	652	659	879	1,226	1,487
Deferred Tax	66	83	82	-9	-25	0	0	0
Tax Rate (%)	33.0	29.0	34.2	31.4	35.2	31.0	35.0	35.0
Add: Associate income	0	0	0	247	160	300	350	350
Reported PAT	753	909	1,185	1,654	1,326	2,256	2,628	3,112
Adjusted PAT	753	909	1,185	1,654	1,326	2,256	2,628	3,112
Change (%)	130.8	20.8	30.3	39.6	-19.8	70.2	16.5	18.4
Margin (%)	6.9	7.0	8.3	11.5	7.8	9.9	10.1	10.2

Consolidated - Balance Sheet

(INR Million)

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E	FY21E
Equity Share Capital	203	204	217	229	254	254	254	254
Total Reserves	3,357	4,107	6,444	8,807	12,788	14,365	15,997	18,115
Net Worth	3,560	4,312	6,660	9,036	13,042	14,618	16,251	18,368
Minority Interest	0	0	0	0	0	0	0	0
Deferred Liabilities	403	549	646	565	543	543	543	543
Total Loans	4,417	4,872	4,767	5,981	9,582	10,082	10,332	10,082
Capital Employed	8,380	9,732	12,074	15,582	23,167	25,244	27,126	28,994
Gross Block	6,539	8,438	9,622	10,099	14,430	15,930	17,730	18,930
Less: Accum. Deprn.	1,714	2,272	2,941	3,656	4,418	5,511	6,790	8,183
Net Fixed Assets	4,825	6,166	6,681	6,443	10,012	10,419	10,940	10,747
Goodwill on Consolidation	0	0	0	0	0	0	0	0
Capital WIP	1,246	620	766	2,605	2,901	3,914	4,475	5,230
Total Investments	2	2	2	1,082	1,566	1,566	1,566	1,566
Curr. Assets, Loans&Adv.	3,848	5,184	7,080	8,633	11,891	13,026	14,535	16,426
Inventory	1,742	2,245	3,071	2,761	2,799	4,660	5,219	6,101
Account Receivables	1,109	1,326	1,526	4,177	6,171	5,941	6,435	7,522
Cash and Bank Balance	418	653	1,419	498	1,156	724	937	531
Loans and Advances	580	959	1,065	1,198	1,765	1,700	1,944	2,272
Curr. Liability & Prov.	1,640	2,295	2,521	3,183	3,272	3,750	4,458	5,044
Account Payables	1,355	1,887	1,791	2,160	2,522	2,071	2,320	2,711
Other Current Liabilities	162	233	608	934	646	971	1,110	1,297
Provisions	123	175	122	89	104	708	1,029	1,036
Net Current Assets	2,208	2,888	4,559	5,451	8,620	9,276	10,077	11,381
Appl. of Funds	8,379	9,732	12,074	15,582	23,167	25,244	27,126	28,994

E: MOSL Estimates

Financials and Valuations

Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E	FY21E
Basic (INR)								
EPS	3.7	4.5	5.5	7.2	5.6	8.9	10.4	12.3
Cash EPS	5.2	7.0	8.4	10.4	8.2	13.2	15.4	17.7
BV/Share	17.6	21.1	30.7	39.5	51.4	57.6	64.0	72.4
DPS	0.4	0.5	0.6	1.0	1.5	2.2	3.3	3.3
Payout (%)	11.0	13.6	13.9	16.2	34.6	30.1	37.9	32.0
Valuation (x)								
P/E	24.8	20.7	16.8	12.7	16.6	10.4	8.9	7.5
Cash P/E	17.8	13.1	10.9	8.9	11.2	7.0	6.0	5.2
P/BV	5.2	4.4	3.0	2.3	1.8	1.6	1.4	1.3
EV/Sales	2.3	2.0	1.7	1.8	1.7	1.3	1.2	1.0
EV/EBITDA	15.8	12.1	8.8	8.9	10.6	7.7	6.2	5.3
Dividend Yield (%)	0.4	0.5	0.7	1.1	1.6	2.4	3.5	3.5
Return Ratios (%)								
RoE	23.9	23.1	21.6	21.1	12.0	16.3	17.0	18.0
RoCE	19.8	18.7	21.4	17.9	11.3	13.2	14.9	16.6
RoIC	15.9	14.6	15.2	14.7	9.1	10.7	12.1	13.6
Working Capital Ratios								
Asset Turnover (x)	1.3	1.3	1.2	0.9	0.7	0.9	1.0	1.1
Inventory (Days)	58	63	78	70	60	75	73	73
Debtor (Days)	36	36	38	104	133	93	88	88
Creditor (Days)	77	92	86	116	103	60	60	60
Leverage Ratio (x)								
Current Ratio	2.3	2.3	2.8	2.7	3.6	3.5	3.3	3.3
Interest Cover Ratio	6	5	5	7	6	10	12	14
Debt/Equity	1.2	1.1	0.7	0.7	0.7	0.7	0.6	0.5

Consolidated - Cash Flow Statement

(INR Million)

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E	FY21E
OP/(Loss) before Tax	1,124	1,280	1,801	2,050	1,800	2,835	3,504	4,250
Depreciation	298	527	643	715	762	1,093	1,279	1,393
Interest & Finance Charges	190	309	347	278	222	-2	150	123
Direct Taxes Paid	-238	-317	-490	-595	-634	-879	-1,226	-1,487
(Inc)/Dec in WC	-310	-363	-915	-557	-2,511	-1,089	-588	-1,711
CF from Operations	1,064	1,435	1,387	1,891	-360	1,958	3,118	2,568
Others	16	18	51	43	0	0	0	0
CF from Operating incl EO	1,080	1,453	1,438	1,934	-360	1,958	3,118	2,568
(inc)/dec in FA	-2,649	-1,473	-1,335	-3,088	-4,626	-2,513	-2,361	-1,956
(Pur)/Sale of Investments	95	0	0	0	-483	0	0	0
Others	8	17	53	-90	108	297	157	183
CF from Investments	-2,546	-1,456	-1,281	-3,178	-5,001	-2,216	-2,204	-1,773
Issue of Shares	11	11	1,059	829	3,139	0	0	0
(Inc)/Dec in Debt	1,709	628	191	151	3,602	500	250	-250
Interest Paid	-205	-319	-406	-319	-331	-295	-306	-306
Dividend Paid	-47	-83	-234	-223	-459	-680	-995	-995
Others	0	0	0	0	68	300	350	350
CF from Fin. Activity	1,467	238	609	438	6,019	-175	-701	-1,201
Inc/Dec of Cash	0	236	766	-805	658	-432	213	-406
Opening Balance	417	417	653	1,303	498	1,156	724	937
Closing Balance	417	653	1,419	498	1,156	724	937	531

E: MOSL Estimates

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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