

Sector: Pharmaceuticals
Result Update

	Change
Reco: Hold	↔
CMP: Rs. 1,469	
Price Target: Rs. 1,720	↔

↑ Upgrade ↔ No change ↓ Downgrade

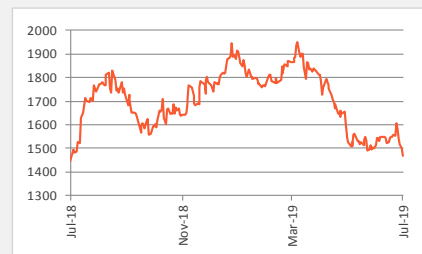
Company details

Market cap:	Rs. 24,973 cr
52-week high/low:	Rs. 1,964/1,407
NSE volume: (No of shares)	2.6 lakh
BSE code:	500420
NSE code:	TORNTPHARM
Sharekhan code:	TORNTPHARM
Free float: (No of shares)	4.9 cr

Shareholding (%)

Promoters	71.3
FII	7.5
DII	11.3
Others	9.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	0.0	-17.0	-21.0	6.7
Relative to Sensex	2.9	-16.1	-24.8	1.2

Sharekhan Research, Bloomberg

Torrent Pharmaceuticals

Operating performance better than expectation; USFDA woes to remain an overhang in the near term

Q1FY2020 result of Torrent Pharmaceuticals Limited (Torrent Pharma) showed strong operational performance. Sales for the quarter were in line with estimates at Rs. 2,022 crore, 8% growth y-o-y. Operating profit was 4% above our estimate at Rs. 541 crore, reporting an improvement of 127 BPS y-o-y to 26.8%. Reported profit for the quarter was 8% above our estimate at Rs. 216 crore, showing robust 32.5% growth y-o-y. During the quarter, U.S. business reported 13% y-o-y growth and no new approvals were received during the quarter. Recently, the company's Dahej plant was classified as Official Action Indicated (OAI) by the USFDA. OAI status does not impact the existing operations of the company, however, new product approvals could get delayed. We feel this event is likely to remain as an overhang in the near term (until successfully closed/resolved).

Key positives

- Strong gross margin of 72.4% (a 220 BPS y-o-y improvement) was reported during the quarter because of better product mix and relaunch of Losar in the U.S. market.
- Operating profit margin (OPM) also improved by 127 BPS to 26.8% during the quarter.
- The company repaid Rs. 330 crore of debt in Q1FY2020 (reducing its gross debt to ~Rs. 5,670 crore).

Key negatives

- USFDA OAI status at Dahej facility to delay product approvals. Management awaits further detailed interaction with USFDA to resolve the issue satisfactorily.

Our Call

Valuation - Maintain Hold with unchanged PT of Rs. 1,720: The stock is currently trading at 15.4x its FY2021E earnings. We expect the company to report sales and adjusted profit CAGR of 17% and 43%, respectively, over FY2019-FY2021E. We feel in the near term, USFDA woes will continue to remain an overhang on the stock price. We have maintained our estimates for FY2020E and FY2021E currently. Due to uncertainty related to USFDA outcome, we continue to maintain our Hold recommendation on the stock with an unchanged PT of Rs. 1,720.

Key Risks

- Slowdown in ANDA approvals and USFDA-related regulatory risks could hurt business prospects.
- Delay in product launches in Brazil, Germany and the U.S. could restrict growth in these key geographies.
- Currency fluctuation poses risk to export businesses.

Valuation

	Rs cr			
Particulars	FY18	FY19	FY20E	FY21E
Net sales	5825.0	7462.0	8450.4	10255.9
OPM (%)	21.0	23.8	24.8	26.2
Adjusted net profit	676.0	793.0	1014.4	1622.8
EPS (Rs.)	39.8	46.6	59.7	95.5
PER (x)	36.9	31.5	24.6	15.4
EV/EBITDA (x)	25.3	17.2	13.2	9.7
P/BV (x)	5.4	5.3	4.4	3.5
Mcap/sales	4.3	3.3	3.0	2.4
Debt:Equity	1.5	1.4	1.0	0.6
ROCE (%)	13.2	12.6	15.8	20.7
RONW (%)	15.1	17.0	19.5	25.3

Source: Company; Sharekhan estimates

Strong operating performance: For Q1FY2020, Torrent Pharma reported 8% y-o-y sales growth, mainly driven by strong growth in domestic and U.S. business. India business for the quarter reported 9% y-o-y growth at Rs. 907 crore (adjusted for base impact of discontinued products, growth was 11% y-o-y). U.S. business reported 12.6% y-o-y growth to Rs. 367 crore for the quarter. Growth in the U.S. was driven by new products (that were launched at the end of Q4FY2019) and relaunch of Losar in the U.S. Gross margin for the quarter improved by 220 BPS to 72.4% due to better product mix. Operating profit grew by 13.4% to Rs. 541 crore, resulting in OPM of 26.8% (127 BPS y-o-y improvement). Profit growth for the quarter was robust at 32.5% y-o-y to Rs. 216 crore. During the quarter, the company reduced gross debt by Rs. 330 crore. Tax rate for FY2020 will be at 23-25%. The company plans to file 15 ANDAs in FY2020.

USFDA regulatory issue at Dahej to weigh on the stock in the near term: Torrent Pharma's Dahej plant was inspected by the USFDA between March 11-19, 2019, and it concluded with the company receiving a Form 483 with five observations (none of them were related to data integrity). USFDA classified this inspection under OAI, indicating unsatisfactory response submitted by the company (for Form 483). OAI status does not impact the existing operations of the company, however, new product approvals could get delayed. If the issue is not resolved satisfactorily within a stipulated timeframe, then it could result in escalation to a Warning Letter/ Import Ban Alert. Hence, we feel this event is likely to remain an overhang in the near term (until successfully closed/resolved). Although the Dahej plant is relatively new, it is strategically important for the company as several new filings come from this unit.

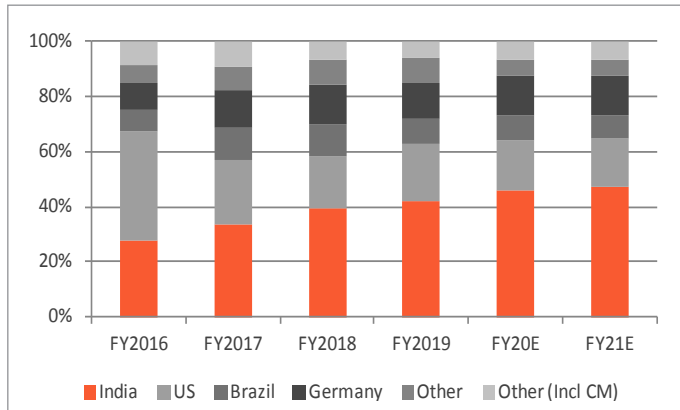
Management confident of USFDA issue resolution: Management stated that since no observations in Form 483 issued by the USFDA relate to data integrity, resolution with USFDA is possible. No new approvals have been granted to the company during the quarter. Management has also stated that if there is delay in resolution, U.S. business growth for FY2020 will be flat but could hurt FY2021 growth. The company is awaiting a further detailed conversation with USFDA for future course of remediation (if any).

Results					Rs cr
Particulars	Q1FY20	Q1FY19	YoY %	Q4FY19	QoQ %
Total Sales	2,022.0	1,872.0	8.0	1,856.0	8.9
Expenditure	1,481.0	1,395.0	6.2	1,383.0	7.1
Operating profit	541.0	477.0	13.4	473.0	14.4
Other income	20.0	27.0	-25.9	17.0	17.6
EBITDA	561.0	504.0	11.3	490.0	14.5
Interest	122.0	122.0	0.0	123.0	-0.8
Depreciation	160.0	150.0	6.7	160.0	0.0
PBT	279.0	232.0	20.3	207.0	34.8
Taxes	63.0	69.0	-8.7	2.0	3050.0
Adjusted PAT	216.0	163.0	32.5	205.0	5.4
Exceptional Item	0.0	0.0		-357.0	
Reported Profit	216.0	163.0	32.5	-152.0	-242.1
EPS (Rs.)	12.7	9.6	32.5	12.1	5.4
Margins			BPS		BPS
OPM %	26.8	25.5	127	25.5	127
EBITDA %	27.7	26.9	82	26.4	134
Adj PATM %	10.7	8.7	198	11.0	-36
Tax %	22.6	29.7	-716	1.0	2,161

Source: Company; Sharekhan Research

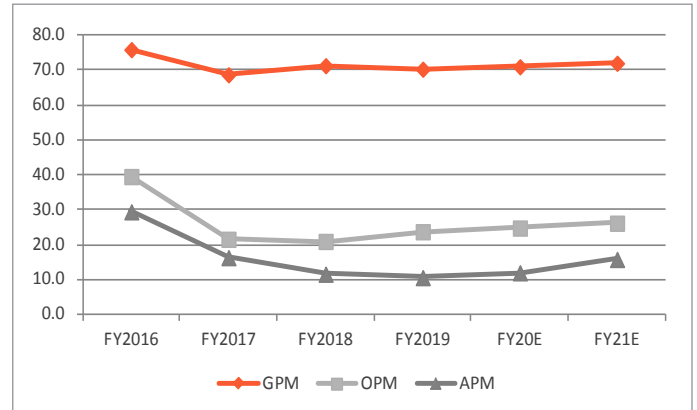
Financials in charts

Geography-wise sales break-up



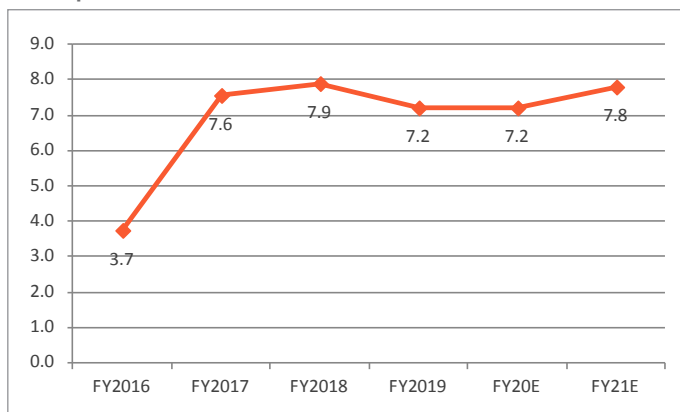
Source: Company, Sharekhan Research

Margin profile



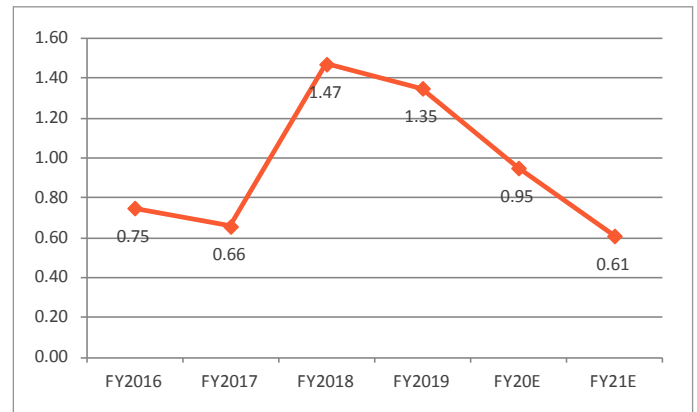
Source: Company, Sharekhan Research

R&D Spend



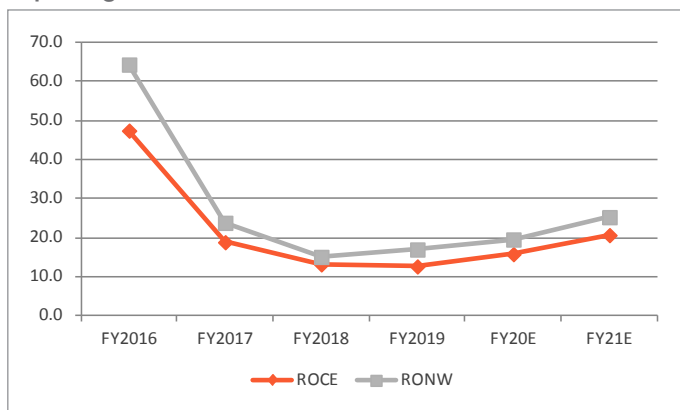
Source: Company, Sharekhan Research

D: E Ratio



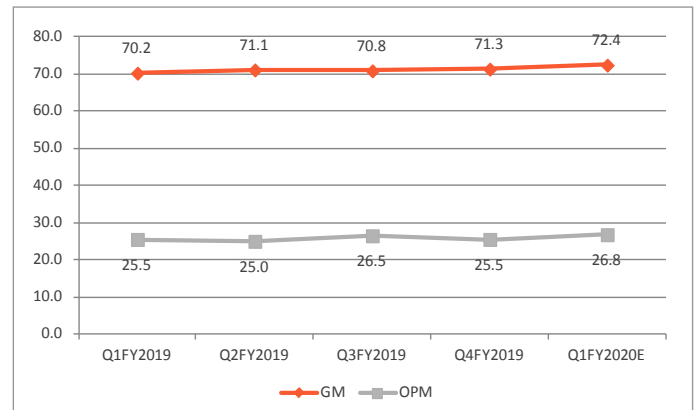
Source: Company, Sharekhan Research

Improving return ratios



Source: Company, Sharekhan Research

Quarterly margin improvement



Source: Company, Sharekhan Research

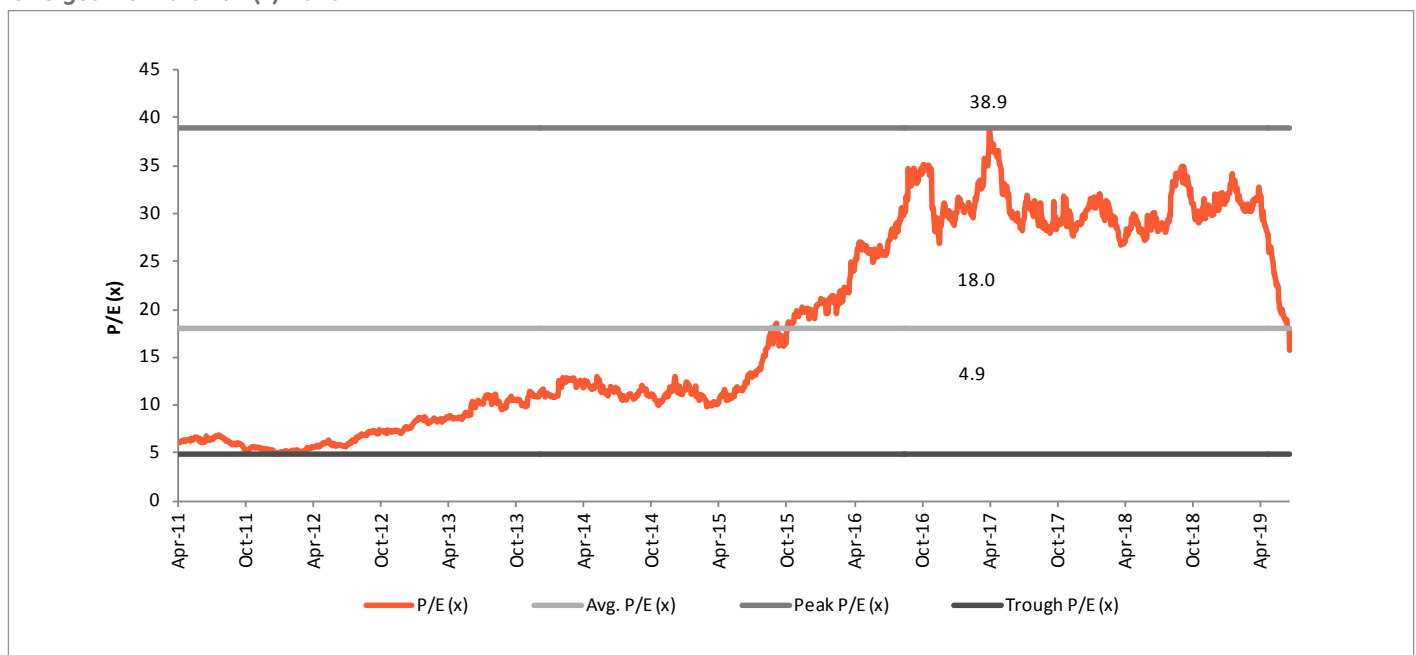
Outlook

Torrent Pharma's operating performance remains strong despite a challenging environment in the U.S. and some slowdown in domestic business. Management stated that since no observations in Form 483 issued by the USFDA relate to data integrity, resolution with USFDA is possible in the near term. We expect the company to report sales and adjusted profit CAGR of 17% and 43%, respectively, over FY2019-FY2021E. We feel in the near term, USFDA woes will continue to remain an overhang on the stock price, until successfully resolved.

Valuation

Torrent Pharma is currently trading at 15.4x its FY2021E earnings, with potential upside of 17% (PT of Rs. 1,720). However, we feel uncertainty related to USFDA outcome of OAI for Dahej facility is likely to remain an overhang in the near term. Hence, we maintain our Hold recommendation on the stock with an unchanged PT of Rs. 1,720.

One-year forward P/E (x) Band



Source: Sharekhan Research

About company

Torrent Pharma, the flagship company of Torrent Group, was incorporated in 1972. Torrent Pharma has a strong international presence across 40 countries with operations in regulated and emerging markets such as the U.S., Europe, Brazil and Rest of the World. The company operates through its wholly owned subsidiaries spread across 12 nations with major setups in Brazil, Germany and the U.S. The company is also one of the leading pharmaceutical companies present in India as a dominant player in the therapeutic areas of cardiovascular (CV) and central nervous system (CNS). The company also has significant presence in gastro-intestinal, diabetology, anti-infective and pain management segments.

Investment theme

Torrent Pharma continues to focus on branded business mix from India and Brazil, which balances well for sustainable growth in a challenging global environment for the pharma sector. U.S. business is also stable. Operating leverage from acquired domestic business is likely to be visible from FY2020.

Key Risks

- ♦ Slowdown in ANDA approvals and USFDA-related regulatory risks could hurt business prospects.
- ♦ Delay in product launches in Brazil, Germany and the U.S. could restrict growth in these key geographies.
- ♦ Currency fluctuation poses risk to export businesses.

Additional Data

Key management personnel

Mr. Sudhir Mehta	Chairman (Emeritus)
Mr. Samir Mehta	Chairman
Mr. Sudhir Menon	CFO
Dr. Chaitanya Dutt	Director (R&D)
Mr. Mahesh Agrawal	VP (Legal) & Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Torrent Pvt. Ltd.	71.25
2	HDFC Asset Management Co. Ltd.	2.61
3	UTI Asset Management Co. Ltd.	1.55
4	Mirae Asset Global Investments Co.	1.44
5	FMR LLC	1.34
6	HDFC Life Insurance Co. Ltd.	1.05
7	SBI Funds Management Pvt. Ltd.	0.93
8	Reliance Capital Trustee Co. Ltd.	0.86
9	Vanguard Group Inc.	0.85
10	T Rowe Price Group Inc.	0.80

Source: Bloomberg

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