

Sun Pharma

Refer to important disclosures at the end of this report

Strong margin beat but US sales plunge

CMP: Rs 532
as of (July 31, 2020)TP: Rs 542 (▲)
12 months

Rating: HOLD (■)

Upside: 1.9 %

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- Sharp cut in opex, lower R&D spends and rise in gross margins boosted EBITDA margins by 765bps qoq to 24.3%. These trends are common across companies. On the other hand, SUNP's US sales fell 25% qoq – the sharpest so far among covered names.
- The US business was largely impacted by a 38% qoq decline in specialty portfolio (at US\$78mn) and 33% in Taro (63% of portfolio is derma, which is one of the severely hit segments). SUNP's own generic business was flat qoq. India growth of +3% yoy beat our estimate of a 3% decline (chronic skew aided).
- Opex cut in Q1 is unlikely to sustain as marketing activity picks up from Q2 onward. With a slow ramp-up in the specialty portfolio, we expect limited margin expansion in the interim due to generic competition in Absorica (Dec'20), increase in India field force (by around 10%) and increase in R&D spends. We expect flat margins over FY20-22E.
- We raise FY22/23E EPS by 5% each and increase the TP to Rs542 as we roll over to 23x Jun'22E EPS (vs. 20x earlier). Higher multiple is on account of the reducing overhang of DOJ penalty with the recent settlement. We retain Hold and UW in EAP.

US miss, but sharp cut in opex drives margin beat: Revenues stood at Rs75.9bn (down 9% yoy/7% qoq), in line with our expectations. The US business plunged 25% to US\$282mn (vs. our estimate of US\$340mn), due to the impact of the lockdown on the specialty portfolio (~38% qoq decline at US\$78mn) and Taro (~33% qoq decline, 63% of portfolio is derma, which is one of the hardest hit segments). SUNP's own generics business was flat qoq. India growth of +3% yoy beat our expectation of a 3% decline (chronic skew aided). API was the other notable segment with 20% yoy growth, similar to what we have seen in other companies. Other common trends were the qoq improvement in gross margins (+220bps qoq), lower other expenses (-750bps qoq) and low R&D spends (-90bps qoq). Consequently, EBITDA margins at 24.3% were 400-500bps above estimates. During the quarter, SUNP also incurred a one-time settlement charge of Rs36.3bn related to the ongoing antitrust litigations in US. Adj. PAT stood at Rs19.8bn vs. our/consensus expectations of Rs5.6bn/Rs10.4bn.

Opex cut may be short-lived: We believe that the sharp cut in opex, is unlikely to sustain as marketing activity picks up across markets with the easing of lockdowns. SUNP expects a partial cut in opex to continue in Q2 as well and then fade off. Further, with a slow ramp-up in the specialty portfolio, we expect limited margin expansion in the interim due to generic competition in Absorica (Dec'20), increase in India field force (by around 10%) and increase in R&D spends.

Retain Hold: We revise FY22/23E EPS up by 5% each. We maintain Hold with a TP of Rs542, valuing the stock at 23x Jun'22E EPS (vs. 20x June'22 EPS earlier). SUNP is an UW in EAP. Key risk: Faster-than-expected ramp up in the specialty portfolio.

Please see our sector model portfolio (Emkay Alpha Portfolio): [Pharmaceuticals \(page 9\)](#)

Financial Snapshot (Consolidated)

(Rs mn)	FY19	FY20	FY21E	FY22E	FY23E
Net Sales	2,90,659	3,28,375	3,48,576	3,83,537	4,16,520
EBITDA	60,276	69,898	78,026	85,531	94,057
EBITDA Margin (%)	20.7	21.3	22.4	22.3	22.6
APAT	34,129	39,734	47,820	54,845	61,919
EPS (Rs)	14.2	16.6	19.9	22.9	25.8
EPS (% chg)	13.0	16.4	20.4	14.7	12.9
ROE (%)	9.1	9.3	10.2	10.6	10.9
P/E (x)	37.4	32.1	26.7	23.3	20.6
EV/EBITDA (x)	21.0	17.7	15.2	13.4	11.6
P/BV (x)	3.1	2.8	2.6	2.4	2.1

Source: Company, Emkay Research



Change in Estimates

EPS Chg FY21E/FY22E (%)	0/5
Target Price change (%)	20
Target Period (Months)	12
Previous Reco	HOLD

Emkay vs Consensus

EPS Estimates		
	FY21E	FY22E
Emkay	19.9	22.9
Consensus	19.8	23.5
Mean Consensus TP (12M)	Rs 508	

Stock Details

Bloomberg Code	SUNP IN
Face Value (Rs)	1
Shares outstanding (mn)	2,399
52 Week H/L	541 / 312
M Cap (Rs bn/USD bn)	1,276 / 17.05
Daily Avg Volume (nos.)	107,69,530
Daily Avg Turnover (US\$ mn)	69.0

Shareholding Pattern Jun '20

Promoters	54.7%
FIIIs	12.7%
DIIIs	20.1%
Public and Others	12.5%

Price Performance

(%)	1M	3M	6M	12M
Absolute	12	14	22	25
Rel. to Nifty	5	2	32	25

Relative price chart



Source: Bloomberg

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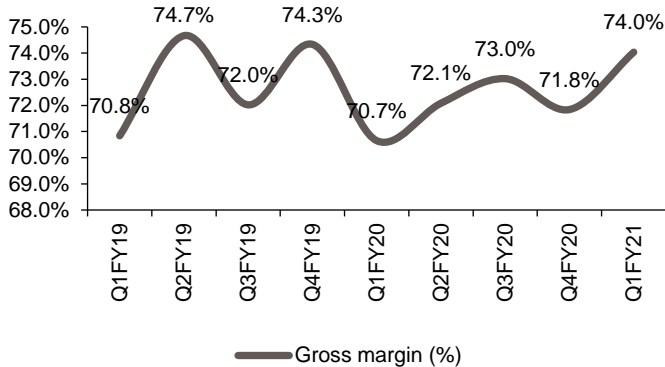
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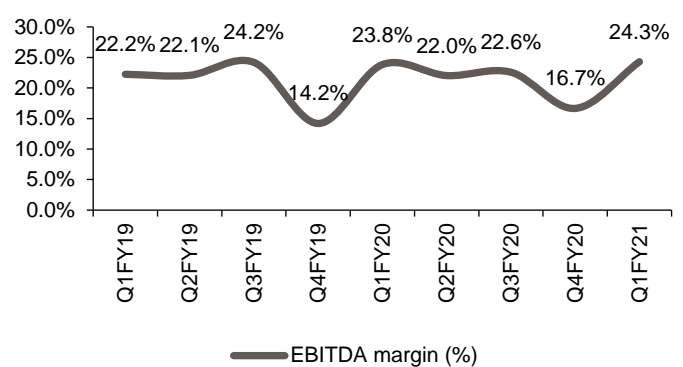
Story in Charts

Exhibit 1: Gross margins were up 220bps qoq



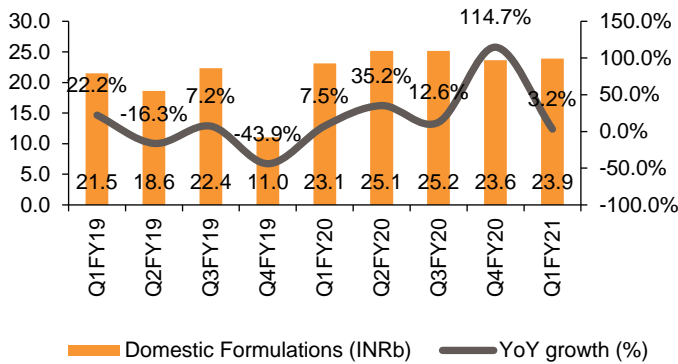
Source: Company

Exhibit 2: EBITDA margins expanded 770bps qoq



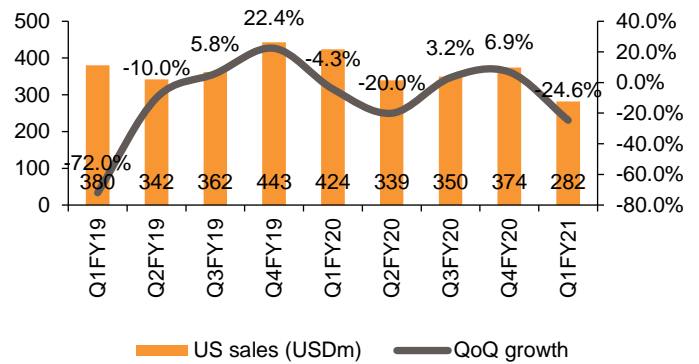
Source: Company

Exhibit 3: Domestic sales fared well despite lockdowns



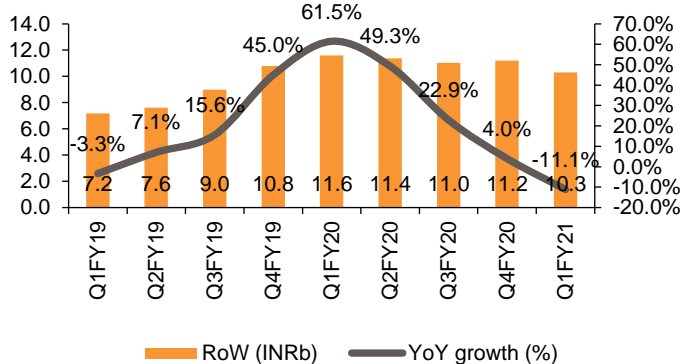
Source: Company

Exhibit 4: US sales declined 25% qoq



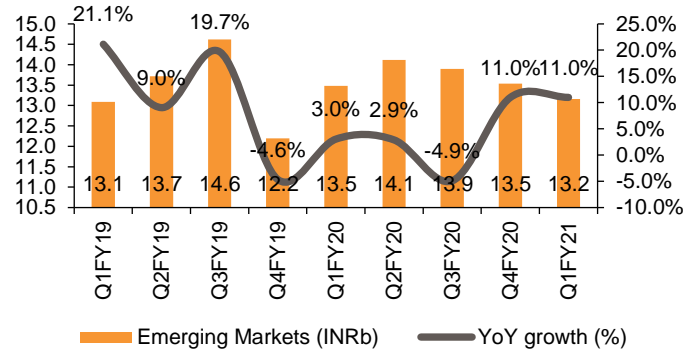
Source: Company

Exhibit 5: RoW sales were down due to lower Japan sales



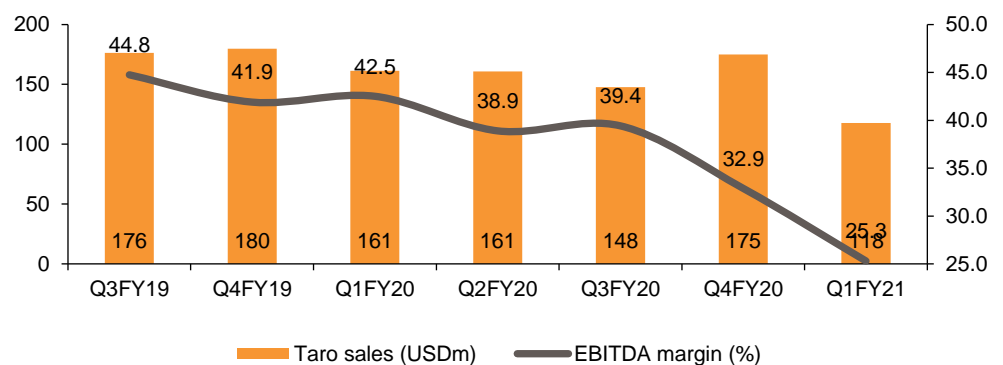
Source: Company

Exhibit 6: EM sales were impacted to lower tender business in SA



Source: Company

Exhibit 7: Taro sales at USD118m were down 33% qoq; EBITDA contracted 760bps qoq



Source: Company

Exhibit 8: Quarterly Snapshot

(Rs mn)	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	YoY (%)	QoQ (%)
Revenue	83,744	81,234	81,549	81,849	75,853	-9.4	-7.3
Consumption of RM	24,578	22,679	22,000	23,048	19,696	-19.9	-14.5
as % of sales	29.3	27.9	27.0	28.2	26.0		
Employee costs	15,404	16,209	15,491	16,519	17,590	14.2	6.5
as % of sales	18.4	20.0	19.0	20.2	23.2		
R&D expense	4,220.0	4,880.0	5,271.3	5,360.0	4,210.0		
as % of sales	5.0	6.0	6.5	6.5	5.6		
Other expenditure	19,586	19,568	20,372	23,292	15,921	-18.7	-31.6
as % of sales	23.4	24.1	25.0	28.5	21.0		
EBITDA	19,956	17,897	18,414	13,630	18,435	-7.6	35.3
Margins (%)	23.8	22.0	22.6	16.7	24.3		
Depreciation	4,571	4,733	5,470	5,754	4,959		
Other Income	2,130	2,009	1,199	1,022	1,538		
Interest	1,041	839	630	518	520		
PBT	16,474	14,334	13,513	8,381	14,494	-12.0	72.9
Total Tax	1,461	2,660	3,276	831	2,459		
Tax rate (%)	8.9	18.6	24.2	9.9	17.0		
PAT before MI	15,014	11,674	10,237	7,550	12,035	-19.8	59.4
Minority interest (MI)	-1,139	-1,033	-1,102	-945	7,742		
Adj. PAT before extraordinary	13,875	10,641	9,135	6,605	19,777	42.5	199.4
Extraordinary expenses	-	-	-	-2,606	-36,333		
Reported PAT	13,875	10,641	9,135	3,998	-16,556	-219.3	-514.1
No. of shrs	2,399	2,399	2,399	2,399	2,399		
EPS	5.8	4.4	3.8	2.8	8.2		

Margins (%)						bps	bps
Gross	70.7	72.1	73.0	71.8	74.0	338	219
EBIDTA	23.8	22.0	22.6	16.7	24.3	47	765
EBIT	20.9	18.7	17.3	10.9	19.8	-112	892
PBT	19.7	17.6	16.6	10.2	19.1	-56	887
Adj. PAT	16.6	13.1	11.2	8.1	26.1	951	1,800
Effective Tax rate	8.9	18.6	24.2	9.9	17.0	810	705

Source: Company

Exhibit 9: Segmental Breakdown

	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	YoY (%)	QoQ (%)
Formulations	77,688	74,533	75,031	75,529	68,709	-11.6	-9.0
Domestic formulation (Rs mn)	23,137	25,148	25,170	23,648	23,884	3.2	1.0
YoY growth (%)	7.5%	35.2%	12.6%	114.7%	3.2%		
US sales (USD mn)	424	339	350	374	282	-33.5	-24.6
QoQ growth	-4.3%	-20.0%	3.2%	6.9%	-24.6%		
RoW (Rs mn)	11,591	11,371	11,035	11,212	10,300	-11.1	-8.1
YoY growth (%)	61.5%	49.3%	22.9%	4.0%	-11.1%		
Emerging market (Rs mn)	13,486	14,117	13,901	13,540	13,161	-2.4	-2.8
YoY growth (%)	3.0%	2.9%	-4.9%	11.0%	11.0%		
API (Rs mn)	4,612	4,681	5,032	4,834	5,537	20.1	14.5
YoY growth (%)	17.0%	9.8%	18.1%	-0.1%	6.0%		
Others (Rs mn)	293	278	324	417	426	45.2	2.0
Total sales (Rs mn)	82,593	79,492	80,387	80,780	74,672	-9.6	-7.6

Source: Company

Exhibit 10: Change in estimates

Change in earnings estimates	FY21			FY22			FY23		
	Old	New	Chng (%)	Old	New	Chng (%)	Old	New	Chng (%)
Revenue	3,53,616	3,48,576	-1.4%	3,83,537	3,83,537	0.0%	4,16,520	4,16,520	0.0%
EBITDA	76,791	78,026	1.6%	82,583	85,531	3.6%	90,822	94,057	3.6%
Margin (%)	21.7	22.4		21.5	22.3		21.8	22.6	
PAT	47,707	47,820	0.2%	52,427	54,845	4.6%	59,266	61,919	4.5%
EPS	19.9	19.9	0.2%	21.9	22.9	4.6%	24.7	25.8	4.5%

Source: Emkay Research

Exhibit 11: Actual vs Estimates

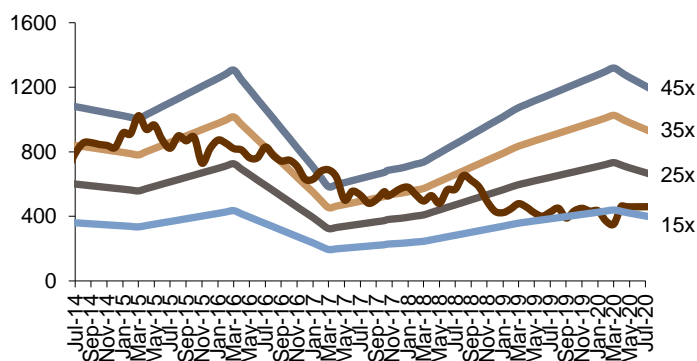
Figures in Rs mn	Actual	Estimate		% Variation		Comments
		Emkay	Consensus	Emkay	Consensus	
Revenue	75,853	77,600	79,932	-2%	-5%	in-line
EBITDA	18,435	13,140	15,991	40%	15%	
EBITDA margin (%)	24.3%	16.9%	20.0%	737	430	Lower other expenses and GM improvement
APAT	19,777	5,581	10425	254%	90%	

Source: Emkay Research

Con-call highlights

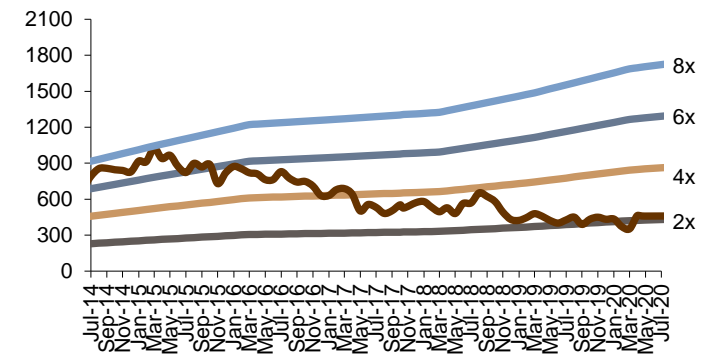
- Overall sales fell 7% sequentially mainly due to a qoq decline in Taro and Specialty sales.
- Efficient management of inventory led to better gross margins.
- Forex gain of Rs790mn vs. forex loss of Rs1.4bn in Q4FY20.
- Other expenses fell due to reduced marketing, selling and travelling across all markets.
- R&D spend for the quarter stood at Rs4.2bn (5.6% of sales). The current generic pipeline includes 95 ANDA and 6 NDA awaiting USFDA approval. 39% of R&D spend was towards the specialty business.
- Specialty revenues stood at USD78mn, impacted by the lockdown as Ilumya and Levulan are clinic administered drugs. However, SUNP has not lost market share in key products.
- Some of the specialty products to break-even by the next year.
- It continues to update USFDA with remediation work. SUNP believes that remediation is almost over but USFDA has not come out with any clear guideline on how to audit a facility which is under OAI status.
- SUNP has received approval for Ilumya in Japan and launch preparations have been initiated. This will be a step in expanding Ilumya globally.
- Domestic branded formulations did well in Q1 despite lockdowns. Chronic saw good traction, but the acute segment faced challenges as clinics were closed. SUNP is engaging with doctors digitally for brand promotion. MR have started field work, barring containment zones.
- SUNP launched ten new products in the Indian market during the quarter. SUNP has 8.2% MS overall in India, according to AIOCD AWACS.
- As per AIOCD, SUNP's chronic portfolio grew 10% yoy, while acute saw a 20-22% decline during the quarter.
- Due to its leadership position in many therapeutic areas, SUNP is the partner of choice for in-licensing.
- It has commenced clinical trials for India of two Covid-19 products. It will possibly announce the result of two studies after two quarters.
- EM sales were down due to the reduction in SA tender business. Adj. sales were flat yoy.
- RoW decline was driven by lower sales in Japan coupled with decrease in Taro sales in RoW markets.

Exhibit 12: P/E chart



Source: Bloomberg

Exhibit 13: P/B chart



Source: Bloomberg

Key Financials (Consolidated)**Income Statement**

Y/E Mar (Rs mn)	FY19	FY20	FY21E	FY22E	FY23E
Net Sales	2,90,659	3,28,375	3,48,576	3,83,537	4,16,520
Expenditure	2,30,383	2,58,477	2,70,550	2,98,006	3,22,462
EBITDA	60,276	69,898	78,026	85,531	94,057
Depreciation	17,533	20,528	22,385	23,585	24,785
EBIT	42,743	49,370	55,641	61,946	69,272
Other Income	10,255	6,360	9,935	12,131	13,139
Interest expenses	5,553	3,027	2,798	3,063	2,769
PBT	47,446	52,702	62,778	71,014	79,642
Tax	6,009	8,228	11,300	12,783	14,336
Extraordinary Items	(9,344)	(2,606)	0	0	0
Minority Int./Income from Assoc.	0	0	0	0	0
Reported Net Income	26,654	37,649	47,820	54,845	61,919
Adjusted PAT	34,129	39,734	47,820	54,845	61,919

Balance Sheet

Y/E Mar (Rs mn)	FY19	FY20	FY21E	FY22E	FY23E
Equity share capital	2,399	2,399	2,399	2,399	2,399
Reserves & surplus	4,11,691	4,45,309	4,88,174	5,37,412	5,93,043
Net worth	4,14,091	4,47,709	4,90,573	5,39,811	5,95,443
Minority Interest	33,135	37,354	41,012	44,399	47,786
Loan Funds	98,934	86,934	79,934	72,934	65,934
Net deferred tax liability	(55,897)	(55,897)	(55,897)	(55,897)	(55,897)
Total Liabilities	4,90,262	5,16,099	5,55,621	6,01,247	6,53,265
Net block	2,18,365	2,12,838	2,05,453	1,96,868	1,87,083
Investment	81,158	81,158	81,158	81,158	81,158
Current Assets	2,75,093	3,10,992	3,70,790	4,33,122	5,02,308
Cash & bank balance	70,623	86,108	1,28,808	1,66,767	2,13,422
Other Current Assets	36,769	51,946	55,141	60,672	65,890
Current liabilities & Provision	98,466	1,01,092	1,13,983	1,22,105	1,29,487
Net current assets	1,76,627	2,09,900	2,56,807	3,11,017	3,72,821
Misc. exp	0	0	0	0	0
Total Assets	4,90,262	5,16,099	5,55,621	6,01,247	6,53,265

Cash Flow

Y/E Mar (Rs mn)	FY19	FY20	FY21E	FY22E	FY23E
PBT (Ex-Other income) (NI+Dep)	37,191	46,343	52,843	58,883	66,503
Other Non-Cash items	0	0	0	0	0
Chg in working cap	(28,437)	(17,787)	(4,208)	(16,252)	(15,148)
Operating Cashflow	21,965	43,882	62,518	56,497	64,574
Capital expenditure	(36,831)	(13,092)	(15,000)	(15,000)	(15,000)
Free Cash Flow	(14,867)	30,790	47,518	41,497	49,574
Investments	10,311	0	0	0	0
Other Investing Cash Flow	9,453	0	0	0	0
Investing Cashflow	(6,813)	(6,732)	(5,065)	(2,869)	(1,861)
Equity Capital Raised	0	0	0	0	0
Loans Taken / (Repaid)	1,416	(12,000)	(7,000)	(7,000)	(7,000)
Dividend paid (incl tax)	(5,787)	(4,031)	(4,956)	(5,606)	(6,288)
Other Financing Cash Flow	(17,382)	0	0	0	0
Financing Cashflow	(27,305)	(19,058)	(14,754)	(15,670)	(16,057)
Net chg in cash	(12,153)	18,092	42,699	37,959	46,656
Opening cash position	79,065	70,623	88,715	1,31,414	1,69,373
Closing cash position	70,623	86,108	1,28,808	1,66,767	2,13,422

Source: Company, Emkay Research

Key Ratios

Profitability (%)	FY19	FY20	FY21E	FY22E	FY23E
EBITDA Margin	20.7	21.3	22.4	22.3	22.6
EBIT Margin	14.7	15.0	16.0	16.2	16.6
Effective Tax Rate	12.7	15.6	18.0	18.0	18.0
Net Margin	14.3	13.5	14.8	15.2	15.7
ROCE	11.1	11.1	12.2	12.8	13.1
ROE	9.1	9.3	10.2	10.6	10.9
RoIC	14.3	14.9	16.6	18.4	20.1

Per Share Data (Rs)	FY19	FY20	FY21E	FY22E	FY23E
EPS	14.2	16.6	19.9	22.9	25.8
CEPS	22.3	25.3	29.3	32.7	36.1
BVPS	172.6	186.6	204.5	225.0	248.2
DPS	1.3	1.6	1.6	1.6	1.6

Valuations (x)	FY19	FY20	FY21E	FY22E	FY23E
PER	37.4	32.1	26.7	23.3	20.6
P/CEPS	24.1	21.2	18.4	16.5	14.9
P/BV	3.1	2.8	2.6	2.4	2.1
EV / Sales	4.4	3.8	3.4	3.0	2.6
EV / EBITDA	21.0	17.7	15.2	13.4	11.6
Dividend Yield (%)	0.3	0.3	0.3	0.3	0.3

Gearing Ratio (x)	FY19	FY20	FY21E	FY22E	FY23E
Net Debt/ Equity	0.0	(0.1)	(0.2)	(0.2)	(0.3)
Net Debt/EBIDTA	(0.2)	(0.6)	(1.1)	(1.6)	(2.0)
Working Cap Cycle (days)	133.1	137.6	134.0	137.3	139.7

Growth (%)	FY19	FY20	FY21E	FY22E	FY23E
Revenue	10.3	13.0	6.2	10.0	8.6
EBITDA	10.0	16.0	11.6	9.6	10.0
EBIT	7.4	15.5	12.7	11.3	11.8
PAT	23.3	41.3	27.0	14.7	12.9

Quarterly (Rs mn)	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21
Revenue	83,744	81,234	81,549	81,849	75,853
EBITDA	19,956	17,897	18,414	13,630	18,435
EBITDA Margin (%)	23.8	22.0	22.6	16.7	24.3
PAT	13,875	10,641	9,135	3,998	(16,556)
EPS (Rs)	5.8	4.4	3.8	1.7	(6.9)

Source: Company, Emkay Research

Shareholding Pattern (%)	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20
Promoters	54.4	54.6	54.6	54.7	54.7
FII	14.9	14.7	13.9	12.8	12.7
DII	18.0	18.5	19.1	19.6	20.1
Public and Others	12.7	12.2	12.5	12.9	12.5

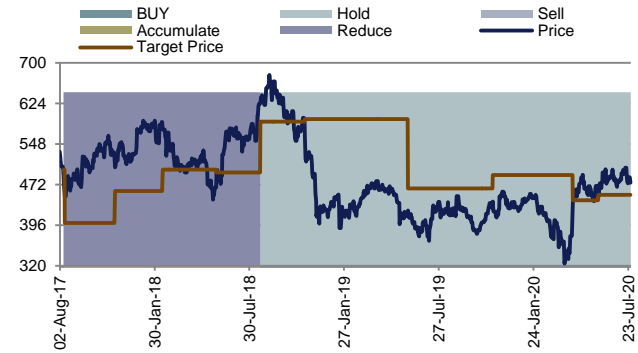
Source: Capitaline

RECOMMENDATION HISTORY TABLE

Date	Closing Price	TP	Period (months)	Rating	Analyst
27-May-20	451	453	12m	Hold	Praful Bohra
08-Apr-20	437	443	12m	Hold	Praful Bohra
07-Feb-20	431	490	12m	Hold	Praful Bohra
20-Dec-19	430	490	12m	Hold	Praful Bohra
16-Dec-19	435	490	12m	Hold	Praful Bohra
07-Nov-19	441	490	12m	Hold	Praful Bohra
19-Aug-19	426	465	12m	Hold	Praful Bohra
13-Aug-19	439	465	12m	Hold	Praful Bohra
29-May-19	424	465	12m	Hold	Praful Bohra
13-Nov-18	562	595	12m	Hold	Jatin Kotian
19-Sep-18	649	590	12m	Hold	Jatin Kotian
03-Sep-18	656	590	12m	Hold	Jatin Kotian
20-Aug-18	626	590	12m	Hold	Jatin Kotian
11-Jul-18	561	495	12m	Reduce	Jatin Kotian
10-Jul-18	564	495	12m	Reduce	Jatin Kotian
29-Jun-18	564	495	12m	Reduce	Jatin Kotian
28-May-18	500	495	12m	Reduce	Jatin Kotian
10-May-18	497	500	12m	Reduce	Jatin Kotian
26-Apr-18	513	500	12m	Reduce	Jatin Kotian
14-Feb-18	575	500	12m	Reduce	Jatin Kotian
15-Nov-17	505	460	12m	Reduce	Jatin Kotian
11-Sep-17	467	400	12m	Reduce	Jatin Kotian
29-Aug-17	482	400	12m	Reduce	Jatin Kotian
11-Aug-17	450	400	12m	Reduce	Jatin Kotian
09-Aug-17	474	500	12m	Reduce	Jatin Kotian

Source: Company, Emkay Research

RECOMMENDATION HISTORY CHART



Source: Bloomberg, Company, Emkay Research

Emkay Alpha Portfolio – Pharmaceuticals

EAP sector portfolio

Company Name	BSE200 Weight	EAP Weight	OW/UW (%)	OW/UW (bps)	EAP Weight (Normalised)
Pharmaceuticals	4.40	4.39	0%	0	100.00
Aurobindo Pharma	0.39	0.44	13%	5	10.00
Cadila Healthcare	0.16	0.15	-3%	0	3.48
Cipla	0.58	0.75	28%	16	17.00
Divi's Lab	0.55	0.40	-27%	-15	9.17
Dr. Reddy's Lab	0.92	0.90	-2%	-2	20.50
Glenmark Pharma	0.11	0.11	-1%	0	2.50
Granules India	0.00	0.45	NA	45	10.28
Ipca Lab	0.20	0.27	37%	7	6.25
Lupin	0.36	0.29	-20%	-7	6.50
Sun Pharma	0.93	0.63	-32%	-30	14.30
Suven Life Sciences*	0.00	0.00	NA	0	0.00
Torrent Pharma	0.20	0.00	-100%	-20	0.00
Cash	0.00	0.00	NA	0	0.0

Source: Emkay Research

* Not under coverage: Equal Weight

■ High Conviction/Strong Over Weight ■ High Conviction/Strong Under Weight

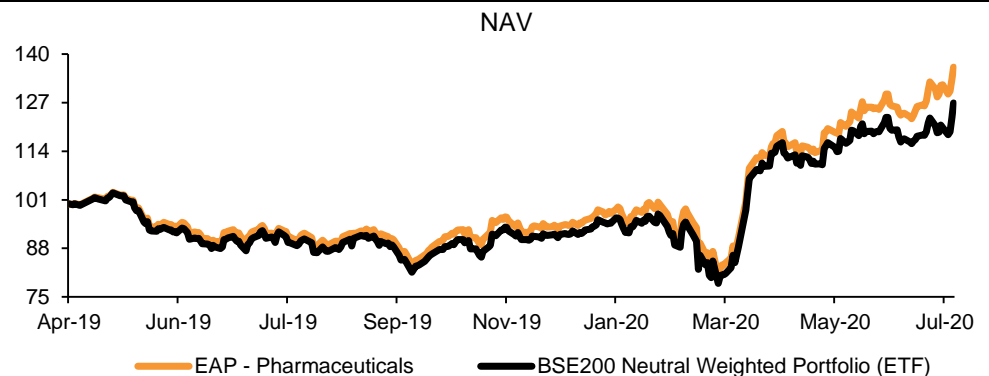
Sector portfolio NAV

	Base					Latest
	1-Apr-19	27-Oct-19	30-Jan-20	30-Apr-20	30-Jun-20	30-Jul-20
EAP - Pharmaceuticals	100.0	91.2	97.3	115.2	124.4	136.5
BSE200 Neutral Weighted Portfolio (ETF)	100.0	88.5	94.5	112.1	117.8	126.9

*Performance measurement base date 1st April 2019

Source: Emkay Research

NAV chart



Source: Emkay Research

Please see our model portfolio (Emkay Alpha Portfolio): [SMID](#)

Please see our model portfolio (Emkay Alpha Portfolio): [Nifty](#)

“Emkay Alpha Portfolio – SMID and Nifty are a supporting document to the Emkay Alpha Portfolios Report and is updated on regular intervals”



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Sector

Pharmaceuticals

Analyst bio

Praful Bohra holds an MBA in Finance and has more than 11 years of experience in equity research. His team currently covers 12 stocks in the Pharmaceuticals space.

Emkay Rating Distribution

Ratings	Expected Return within the next 12-18 months.
BUY	Over 15%
HOLD	Between -5% to 15%
SELL	Below -5%

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