

18 August 2020

Suven Pharmaceuticals

Strong Q1 'mid headwinds, profitability to rise; retaining a Buy

Rating: **Buy**

Target Price: ₹760

Share Price: ₹652

Strong, 39%, growth in its CDMO pharma to ₹1.3bn led to Suven's Q1 FY21 sales rising 20.7% y/y to ₹2.4bn. The unfavourable product mix, however, pulled the gross margin down 875bps to 70.3%. But operating leverage helped curtail the EBITDA margin decline (down 486bps y/y) to 47%. On the lower share of profit from the Rising Pharma JV and the higher tax rate, PAT was flat at ₹915m. Suven is on track in launching molecules (two in specialty chemicals over FY21-22 and one in pharma) in CDMO and in filing formulation products (six pending approval, another five being developed). Traction in its CDMO business and steady formulation launches would drive 17.3%/19.2% growth in sales/ earnings over FY20-23. We retain our Buy recommendation with a higher target of ₹760 (earlier ₹695).

Commercial products continue to fuel CDMO growth. The Covid-19 outbreak halted new projects in pharma and we believe the Q1 39% growth was largely driven by the four products in the commercial phase. In specialty CRAMS, the company supplies intermediates for two molecules; here, sales slipped 3.5% to ₹970m in Q1 FY21. Management is confident of adding one more specialty chemical molecule in FY21. We expect 14%/16.1% CAGRs in its CDMO pharma/specialty chemicals divisions over FY20-23.

Launches to increase formulation sales. Sales of formulations brought ₹40m in Q1 FY21. The company has so far launched two products and plans to add one in FY21. In FY22 it plans to launch 3-4 products. It has a niche focus in formulations as it works on a profit-sharing model and expects margins in this segment to be in line with its existing CRAMS business. We expect its formulations and other services to grow 34.4% over FY20-23.

Valuation. At the CMP of ₹652, the stock trades at 22.1x, 18.3x and 15.5x respective FY21e/22e/23e earnings. We retain our Buy recommendation, with a higher price target of ₹760 (earlier ₹695), based on 18x FY23e EPS. **Risks:** Currency fluctuations, delay in new orders from clients.

Key financials (YE Mar)	FY19	FY20	FY21e	FY22e	FY23e
Sales (₹ m)	6,635	8,338	9,520	11,311	13,474
Net profit (₹ m)	1,978	3,170	3,760	4,535	5,366
EPS (₹)	15.5	24.9	29.5	35.6	42.2
PE (x)	42.0	26.2	22.1	18.3	15.5
EV / EBITDA (x)	28.5	21.9	18.9	15.4	12.2
PBV (x)	10.0	9.8	7.3	5.6	4.4
RoE (%)	24.8	37.8	38.1	34.8	32.0
RoCE (%)	23.0	30.1	29.3	29.4	28.3
Dividend yield (%)	0.5	0.8	0.9	-	-
Net debt / equity (x)	-0.2	0.2	-0.0	-0.2	-0.4

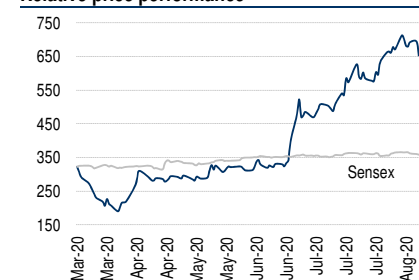
Source: Company, Anand Rathi Research

Key data	SUVENPHA IN
52-week high / low	₹750 / 174
Sensex / Nifty	38528 / 11385
3-m average volume	\$2.7m
Market cap	₹83bn / \$1111.5m
Shares outstanding	127m

Shareholding pattern (%)	Jun'20	Mar '20
Promoters	60.0	60.0
- of which, Pledged	-	-
Free float	40.0	40.0
- Foreign institutions	3.6	4.2
- Domestic institutions	4.6	4.0
- Public	31.8	31.8

Estimates revision (%)	FY21e	FY22e	FY23e
Sales	2.7	2.6	2.3
EBITDA	2.7	2.6	2.2
EPS	2.2	2.1	2.1

Relative price performance



Source: Bloomberg

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Quick Glance – Consolidated Financials and Valuations

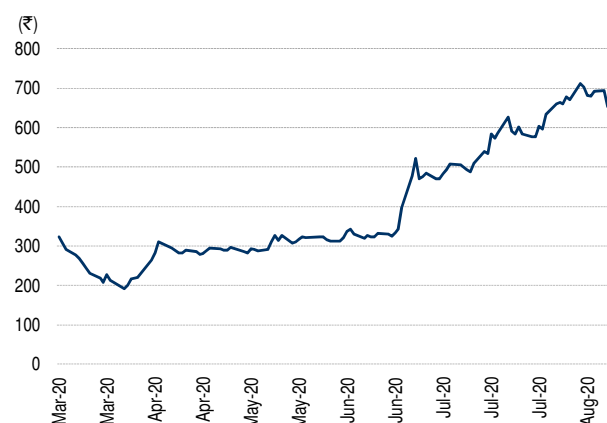
Fig 1 – Income statement (₹ m)

Year-end: Mar	FY20	FY21e	FY22e	FY23e
Net revenues	8,338	9,520	11,311	13,474
Growth (%)	25.7	14.2	18.8	19.1
Direct costs	2,292	2,618	3,110	3,705
SG&A	2,198	2,523	2,997	3,544
EBITDA	3,848	4,379	5,203	6,225
EBITDA margins (%)	46.1	46.0	46.0	46.2
- Depreciation	235	285	326	376
Other income	181	362	453	510
Interest expenses	231	64	-	-
PBT	482	554	638	701
Effective tax rate (%)	4,045	4,947	5,968	7,060
+ Associates / (Minorities)	21.6	24.0	24.0	24.0
Net income	3,170	3,760	4,535	5,366
Adjusted income	3,170	3,760	4,535	5,366
WANS	127	127	127	127
FDEPS (₹ / sh)	24.9	29.5	35.6	42.2
R&D (% of sales)	8,338	9,520	11,311	13,474

Fig 3 – Cash-flow statement (₹ m)

Year-end: Mar	FY20	FY21e	FY22e	FY23e
PBT	4,045	4,947	5,968	7,060
+ Non-cash items	235	285	326	376
Oper. prof. before WC	4,280	5,232	6,294	7,436
- Incr. / (decr.) in WC	-220	444	536	183
Others incl. taxes	888	1,187	1,432	1,694
Operating cash-flow	3,613	3,600	4,325	5,558
- Capex (tang. + intang.)	776	1,000	500	500
Free cash-flow	2,836	2,600	3,825	5,058
Acquisitions				
- Div. (incl. buyback & taxes)	763	905	1,092	1,292
+ Equity raised	-	-	-	-
+ Debt raised	1,482	-913	-950	-
- Fin investments	1,081	-	-	-
- Misc. (CFI + CFF)	2,469	(0)	(0)	0
Net cash-flow	5	783	1,784	3,766

Source: Company, Anand Rathi Research

Fig 5 – Price movement


Source: Bloomberg

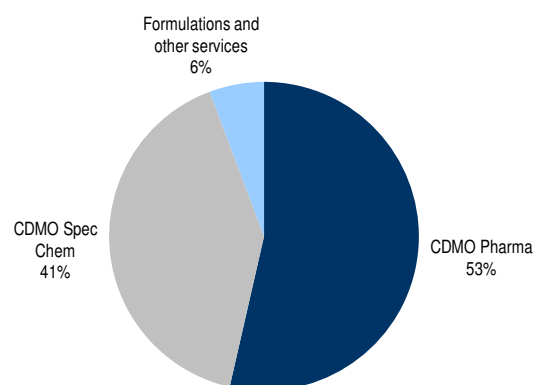
Fig 2 – Balance sheet (₹ m)

Year-end: Mar	FY20	FY21e	FY22e	FY23e
Share capital	127	127	127	127
Net worth	8,448	11,302	14,746	18,820
Debt	1,862	950	-	-
Minority interest	-	-	-	-
DTL / (Assets)	276	276	276	276
Capital employed	10,586	12,528	15,022	19,096
Net tangible assets	3,539	4,498	5,217	5,887
Net intangible assets	28	35	40	44
Goodwill	-	-	-	-
CWIP (tang. & intang.)	1,017	767	217	-333
Investments (strategic)	3,075	3,075	3,075	3,075
Investments (financial)	307	307	307	307
Current assets (ex cash)	3,622	4,324	5,103	5,475
Cash	141	923	2,707	6,473
Current liabilities	1,142	1,400	1,643	1,832
Working capital	2,479	2,924	3,460	3,643
Capital deployed	10,586	12,528	15,022	19,096
Contingent liabilities	-	-	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY20	FY21e	FY22e	FY23e
P/E (x)	26.2	22.1	18.3	15.5
EV / EBITDA (x)	21.9	18.9	15.4	12.2
EV / Sales (x)	10.1	8.7	7.1	5.7
P/B (x)	9.8	7.3	5.6	4.4
RoE (%)	37.8	38.1	34.8	32.0
RoCE (%) - after tax	30.1	29.3	29.4	28.3
DPS (₹ / sh)				
Dividend yield (%)	5.0	5.9	-	-
Dividend payout (%) - incl. DDT	0.8	0.9	-	-
Net debt / equity (x)	24.1	24.1	24.1	24.1
Receivables (days)	0.2	-0.0	-0.2	-0.4
Inventory (days)	51	57	57	48
Payables (days)	77	70	69	68
CFO : PAT %	31	32	32	32

Source: Company, Anand Rathi Research

Fig 6 – Revenue break-up (Q1 FY21)


Source: Bloomberg

Result highlights

Fig 7 – Quarterly financials

(₹ m)	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	% Y/Y	% Q/Q
Sales	1,269	2,509	1,974	2,729	1,787	1,848	2,382	20.7	28.9
Gross profit	991	1,755	1,560	1,819	1,349	1,318	1,675	7.3	27.1
Gross margins (%)	78.1	70.0	79.1	66.6	75.5	71.3	70.3	-875bps	-103bps
EBITDA	495	1,220	1,025	1,256	796	773	1,121	9.4	45.1
EBITDA margins (%)	39.0	48.6	51.9	46.0	44.6	41.8	47.0	-486bps	523bps
Finance expenses	10	17	38	44	76	72	32	(16.0)	(55.6)
Depreciation	55	60	55	56	56	70	71	28.5	1.4
Other income	2	4	24	54	49	53	57	134.8	7.5
PBT	431	1,147	1,130	1,210	777	894	1,179	4.4	31.9
Tax	87	399	210	315	198	152	263	25.2	73.3
Effective tax rate (%)	20	35	19	26	25	17	22	20.0	31.5
Adjusted PAT	345	748	919	895	579	742	915	(0.4)	23.4

Source: Company, Anand Rathi Research

Fig 8 – Revenue break-up

(₹ m)	Q3 FY19	Q4 FY19	Q1 FY20	Q2 FY20	Q3 FY20	Q4 FY20	Q1 FY21	% Y/Y	% Q/Q
CDMO pharma	850	1,138	918	2,060	792	910	1,276	39.0	40.2
% of sales	67.5	45.9	46.1	75.5	42.8	49.3	53.6		
CDMO specialty chemicals	270	1,180	1,005	540	695	800	970	(3.5)	21.3
% of sales	21.4	47.6	50.5	19.8	37.5	43.3	40.7		
Formulations and other services	140	159	67	130	365	138	136	103.0	(1.2)
% of sales	11.1	6.4	3.4	4.8	19.7	7.4	5.7		
Total	1,260	2,477	1,990	2,730	1,852	1,848	2,382	19.7	28.9

Source: Company, Anand Rathi Research

Concall highlights, Key takeaways

Guidance

- Management has raised its FY21 profit growth guidance. On a standalone level (excl. the profit share of Rising Pharma) it now expects 10-15% topline growth in FY21, and 20% in PAT (earlier 10-15%).
- Management is confident of at least a 40% EBITDA margin in FY21.
- On the Covid-19 outbreak, new project flows have been hit; recovery is expected from Sep/Oct.
- The profit share from the Rising Pharma JV can range between ₹400m and ₹600m in FY21.
- Growth drivers for Q2 FY21 will be similar to those for Q1, while new order inflows are expected to improve from Q3 FY21.

Pharma CRAMS

- The company has 60-70 projects in the clinical stage for ~40 customers.
- It hasn't lost any molecule in the clinical trials in CRAMS due to outbreak of Covid-19.
- Customer stickiness increases when a molecule enters phase-2 trials.
- The company does not anticipate any benefits from the current disruption in China.

Specialty CRAMS

- The company is on track to commercialize one more product in FY21.
- 90% of specialty chemical molecules are for agro chemicals.

Formulations

- Formulations sales in Q1 were ₹40m. The company supplies two formulations products currently and plans to add one more in FY21. Further, it is developing five products.
- It plans to further commercialize 3-4 products in FY22.
- The share of profit of formulations products supplied in Q1 is expected to come in Q2.

Cash transfer to Suven Lifesciences

- At 30th Jun'20, Suven Pharma had to repay ₹1.15bn to Suven Lifesciences.
- Of this, it will pay ₹410m in FY21 and the rest in 12-18 months.
- On 30th Jun'20, its cash balance was ₹400m.

Capex

- It had spent ₹300m in Q1 FY21 and envisages capex of nearly ₹1.2bn for FY21 (₹900m in the remaining nine months).
- It is spending ₹1bn on the new Vishakhapatnam plant, expected to be commercialized by end-CY22.

Other highlights

- Q1 FY20 sales break-up: pharma CRAMS ₹920m, specialty chemicals ₹1bn, formulations and other services ₹70m.
- Its plans to bring in professional management have been delayed by the pandemic. Management's priority now is to ensure business stability.
- Billing in the Services division is done once in 6-9 months; hence, sales in this division may be lumpy on a quarterly basis.

Fig 9 – Sales break-up assumptions

₹m)	FY21e	FY22e	FY23e
CDMO Pharma	5,228	6,196	6,966
% Y/Y	11.7	18.5	12.4
% of Sales	55.0	54.9	51.8
CDMO Specialty Chemicals	3,404	3,915	4,776
% Y/Y	12.0	15.0	22.0
% of Sales	35.8	34.7	35.5
Formulations and other services	875	1,181	1,713
% Y/Y	25.0	35.0	45.0
% of Sales	9.2	10.5	12.7
Total	9,507	11,292	13,455

Source: Company, Anand Rathi Research

Valuations

Considering the better-than-anticipated performance in its CDMO pharma division, we raise our FY21e, FY22e and FY23e earnings, respectively 2.2%, 2.1% and 2.1%.

Fig 10 – Change in estimates

₹ m	Old estimates			New estimates			Change (%)		
	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e
Revenue	9,271	11,028	13,177	9,520	11,311	13,474	2.7	2.6	2.3
EBITDA	4,265	5,073	6,088	4,379	5,203	6,225	2.7	2.6	2.2
PAT	3,678	4,442	5,257	3,760	4,535	5,366	2.2	2.1	2.1

Source: Anand Rathi Research

Suven is on track in launching molecules (two in specialty chemicals over FY20-22 and one in pharma) in CDMO and in filing formulation products (six pending approval, another five being developed). Traction in its CDMO division and steady formulation launches would drive 17.3%/19.2% growth in sales/ earnings over FY20-23. We retain our Buy recommendation with a higher target of ₹760 (earlier ₹695).

Risks

- Currency fluctuations
- Regulatory hurdles on any plant
- Delay in orders from clients.

Fig 11 – Key data

	RATING	CMP (₹)	TP (₹)	M Cap (₹ bn)	EPS (₹)			PE (x)			EV / EBITDA			RoE (%)		
					FY21e	FY22e	FY23e	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e
Aarti Drugs	Buy	2367	2090	49.2	101.9	112.4	144.0	23.2	21.1	16.4	10.9	9.8	7.5	31.0	26.1	26.0
Ajanta	Hold	1682	1614	412.2	57.8	73.2	87.8	29.1	23.0	19.2	14.4	12.3	13.3	18.8	19.1	20.1
Alembic	Hold	1009	985	204.6	45.6	46.6	53.0	22.1	21.6	19.1	15.8	14.8	12.9	24.3	21.0	20.4
Alkem	Hold	2891	3145	352.6	106.0	123.9	136.8	27.3	23.3	21.1	21.2	17.9	15.9	19.2	19.6	18.9
Zydus Cadila	Hold	397	431	404.8	15.1	17.5	19.6	26.4	22.7	20.3	15.9	14.0	12.4	14.3	15.3	15.5
Eris	Hold	525	565	73.8	24.2	26.0	27.9	21.7	20.2	18.8	17.7	15.8	14.0	23.0	20.9	19.2
Granules India	Buy	306	330	75.9	17.5	21.8	27.2	17.5	14.1	11.2	9.9	7.9	6.1	21.8	22.4	23.0
Indoco Remedies	Sell	255	190	22.7	7.5	10.3	12.5	33.8	24.7	20.4	13.7	11.1	9.5	9.7	12.0	12.9
Ipca Labs.	Buy	2004	2300	254.3	87.6	90.8	103.5	22.9	22.1	19.4	16.2	15.2	12.9	26.9	22.4	21.0
JB Chemicals	Sell	779	720	61.5	37.5	43.7	49.8	20.8	17.8	15.6	12.4	10.3	8.6	18.9	19.2	19.2
Natco Pharma	Hold	814	837	151.0	28.1	31.0	75.7	29.0	26.3	10.8	22.9	19.8	8.0	12.8	12.7	26.3
Neuland	Hold	862	795	10.3	36.7	44.5	53.0	23.5	19.4	16.3	7.6	6.0	7.0	4.1	6.1	7.1
Pfizer	Hold	4576	4449	205.2	110.3	122.9	132.0	41.5	37.2	34.7	27.1	24.1	21.8	14.1	14.1	13.7
Suven Pharma	Buy	652	760	88.3	29.5	35.6	42.2	22.1	18.3	15.5	18.9	15.4	12.2	38.1	34.8	32.0
Torrent Pharma	Buy	2805	2995	480.4	66.0	82.0	100.6	42.5	34.2	27.9	19.7	16.4	16.4	21.7	23.7	25.2

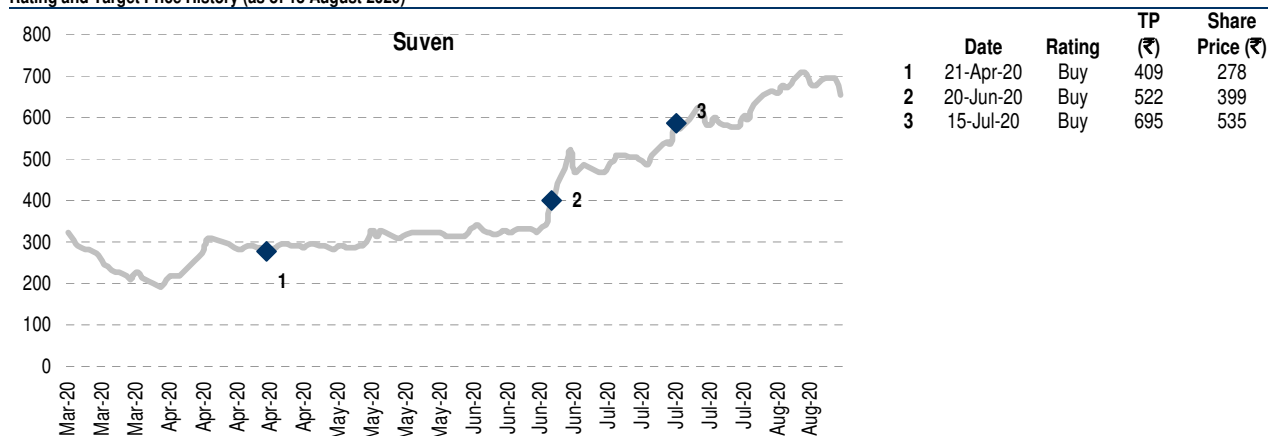
Source: Company, Anand Rathi Research

Appendix

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