

Reduce

Q2 in-line, priced to perfection

- In 2QFY21, Torrent reported muted performance in its key export markets – US (20% YoY decline), Brazil (17% YoY decline, primarily due to currency depreciation) while India (7% YoY growth) aided in flattish revenues for the quarter, in-line with our estimates. However, EBITDA margin at 31.5% were marginally better than expectation led by controlled fixed costs. With field activities resuming normalcy (~75-80% in both Indian and Brazilian market), we expect cost structure to normalize in next 2 quarters.
- US business (impacted by lack of new launches, temporary discontinuation of sartans and higher price erosion on base portfolio) is expected to remain muted in 2HFY21 as well. Levittown facility is expected to start commercialization from Mar'21, while the company awaits USFDA inspection at its Dahej and Inrad facilities. SOP upgradation in Germany is largely completed and should see gradual improvement from 3Q onwards. Nonetheless, we believe the focus should remain primarily on the domestic market, which is likely to account for 68% of its FY23E EBITDA, with US contribution expected to come down to 6% of FY23 EBITDA. While Torrent has delivered impressive growth in India led by synergistic acquisitions, we believe growth levers from India business has been captured largely and margins have peaked for Torrent as current valuation leaves limited room for an upside. Focus will now shift to growth and balance sheet de-leveraging (debt reduction of Rs4.4bn in 1H vs guidance of Rs10bn in FY21). We estimate earnings CAGR of 20% in FY21-23.
- At CMP, stock trades at 32x FY22 and 27x FY23 EPS of Rs84.4 and Rs99.6 respectively. Given the higher contribution from branded markets (~60% of revenue), higher exposure to chronic therapies in domestic business and healthy FCF (~Rs8bn in FY20-23E), we value Torrent at ~20% premium to other large cap pharma stocks. Our target price of Rs2,863 is 28x FY23 EPS of Rs99.6 Maintain Reduce.

Q2FY21 Result (Rs Mn)

Particulars	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)
Revenue	20,170	20,050	0.6	20,560	(1.9)
Total Expense	13,820	14,640	(5.6)	13,950	(0.9)
EBITDA	6,350	5,410	17.4	6,610	(3.9)
Depreciation	1,650	1,630	1.2	1,610	2.5
EBIT	4,700	3,780	24.3	5,000	(6.0)
Other Income	60	340	(82.4)	40	50.0
Interest	920	1,160	(20.7)	1,020	(9.8)
EBT	3,840	2,960	29.7	4,020	(4.5)
Tax	740	520	42.3	810	(8.6)
RPAT	3,100	2,440	27.0	3,210	(3.4)
APAT	3,100	2,440	27.0	3,210	(3.4)
			(bps)		(bps)
Gross Margin (%)	72.5	73.2	(63)	74.0	(145)
EBITDA Margin (%)	31.5	27.0	450	32.1	(67)
NPM (%)	15.4	12.2	320	15.6	(24)
Tax Rate (%)	19.3	17.6	170	20.1	(88)
EBIT Margin (%)	23.3	18.9	445	24.3	(102)

CMP	Rs 2,657
Target / Upside	Rs 2,863 / 8%
NIFTY	11,930

Scrip Details

Equity / FV	Rs 846mn / Rs 5
Market Cap	Rs 450bn
	USD 6bn
52-week High/Low	Rs 3,031/ 1,583
Avg. Volume (no)	831,347
Bloom Code	TRP IN

Price Performance

	1M	3M	12M
Absolute (%)	(2)	16	52
Rel to NIFTY (%)	(10)	10	49

Shareholding Pattern

	Mar'20	Jun'20	Sep'20
Promoters	71.3	71.3	71.3
MF/Banks/FIs	10.9	10.9	11.0
FIIs	9.8	9.8	9.8
Public / Others	8.1	8.1	8.0

Valuation (x)

	FY21E	FY22E	FY23E
P/E	38.4	31.5	26.7
EV/EBITDA	19.6	17.6	15.5
ROE (%)	22.7	24.1	24.2
RoACE (%)	15.7	16.8	17.6

Estimates (Rs mn)

	FY21E	FY22E	FY23E
Revenue	84,192	92,357	101,406
EBITDA	24,356	26,334	28,975
PAT	11,698	14,284	16,855
EPS (Rs.)	69.1	84.4	99.6

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Exhibit 1: Revenue Mix

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	1HFY21	1HFY20	YoY (%)	FY21	FY20	YoY (%)
India	9,630	8,990	7.1	9,250	4.1	18,880	18,060	4.5	37,954	35,170	7.9
Brazil	1,290	1,560	(17.3)	1,400	(7.9)	2,690	3,300	(18.5)	7,301	7,150	2.1
US	3,270	3,800	(13.9)	3,730	(12.3)	7,000	7,560	(7.4)	13,957	15,230	(8.4)
Germany	2,610	2,500	4.4	2,460	6.1	5,070	5,120	(1.0)	9,984	9,470	5.4
RoW	2,000	1,940	3.1	2,340	(14.5)	4,340	3,700	17.3	8,229	7,660	7.4
Others	1,390	1,260	10.3	1,380	0.7	2,770	2,530	9.5	5,181	4,720	9.8
Total Income	20,190	20,050	0.7	20,560	(1.8)	40,750	40,270	1.2	82,606	79,400	4.0

Source: Company, DART

Concall highlights

- Domestic formulations:** Torrent recorded 5% growth in its chronic segment vs 1% growth in IPM, while its sub-chronic business de-grew 6% in Q2. Overall the company recorded 7% growth vs a 1% growth in IPM. The quarter continued to witness strong growth in key brands such as Shelcal, Losar and Ampoxin. However large part of the growth has been led by price hikes 7% and 2% by new launches as volumes continue to remain negative in Q2. With 10 brands above Rs1bn sales, Torrent's fairly strong chronic product profile is likely to be less impacted. Further, management has continuously improved its productivity and now generates Rs8mn PCPA. Management targets to achieve Rs10mn PCPA in the next 2-3 years.
- US business:** The US business declined 20% YoY on constant currency basis at US\$43mn. Sales was impacted due to lack of new launches, temporary discontinuation of sartans and higher price erosion on base portfolio. Levittown facility will start commercialization from Mar'21. Torrent expects to launch few products from Derma facility or external partners. The company awaits USFDA inspection at its Dahej and Inrad facilities. It indicated that US continues to remain competitive as panic buying is over.
- Germany:** Tenders contribute 60% to Torrent's Germany revenue, followed by out-of-tender (30%) and OTC businesses (10%). As system upgradation exercise is completed, management expects the situation to rebound from 2H onwards.
- Brazil:** Though on a constant currency basis, Torrent grew 5% in 2Q, local currency depreciation led to 17% decline YoY. Management remains confident of growing ahead of the market growth, with the focus on specialty areas, augmenting distribution channels, and enhancing MR productivity with new product additions. It guided for 3 launches and 3 filings in FY21E.

Operational performance: Torrent reported 9% QoQ decline in fixed expenses in Q2 despite higher ongoing field activities vs Q1. Management cited certain one-off costs such freight charges, donation to PM fund in Q1 which led to higher expenses in Q1. Nonetheless, with 85% of MRs back on the field we expect operational performance to normalize in subsequent quarters. Capitalization of employee expenses (to the tune of Rs100-110mn) w.r.t US facility under upgradation will continue for another 1-2 quarters. Further, management now maintains high inventory levels (~12 months' vs 3-4 months earlier) to safeguard itself from supply chain disruptions amid the pandemic. In line with its guidance of debt reduction of Rs10bn in FY21E, company has repaid Rs4.4bn in 1H. Net debt now stands at Rs42bn vs Rs50bn in Q1.

Profit and Loss Account

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Revenue	79,393	84,192	92,357	101,406
Total Expense	57,690	59,836	66,023	72,431
COGS	21,669	23,655	25,468	27,554
Employees Cost	14,290	15,282	16,332	17,753
Other expenses	21,730	20,899	24,223	27,124
EBIDTA	21,704	24,356	26,334	28,975
Depreciation	6,544	6,632	6,821	6,963
EBIT	15,160	17,725	19,513	22,012
Interest	4,507	3,632	2,236	1,377
Other Income	1,213	1,100	1,035	975
Exc. / E.O. items	0	0	0	0
EBT	11,866	15,192	18,312	21,610
Tax	1,619	3,494	4,029	4,754
RPAT	10,247	11,698	14,284	16,855
Minority Interest	0	0	0	0
Profit/Loss share of associates	0	0	0	0
APAT	10,247	11,698	14,284	16,855

Balance Sheet

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Sources of Funds				
Equity Capital	846	846	846	846
Minority Interest	0	0	0	0
Reserves & Surplus	47,386	53,875	62,951	74,598
Net Worth	48,232	54,722	63,797	75,444
Total Debt	43,947	33,947	27,947	22,947
Net Deferred Tax Liability	6,262	8,202	8,494	8,795
Total Capital Employed	98,441	96,871	100,238	107,185

Applications of Funds

Net Block	70,556	67,146	63,223	58,434
CWIP	11,894	11,165	11,266	11,342
Investments	2,220	2,330	2,445	2,567
Current Assets, Loans & Advances	55,708	54,426	63,764	76,890
Inventories	21,482	20,835	21,367	22,734
Receivables	16,493	16,747	16,158	17,488
Cash and Bank Balances	6,667	5,753	14,804	24,644
Loans and Advances	6,471	6,564	6,713	7,105
Other Current Assets	4,594	4,526	4,723	4,918
Less: Current Liabilities & Provisions	41,937	38,196	40,461	42,048
Payables	20,769	18,911	20,657	21,790
Other Current Liabilities	21,168	19,286	19,804	20,257
		<i>sub total</i>		
Net Current Assets	13,771	16,230	23,303	34,842
Total Assets	98,441	96,871	100,238	107,185

E – Estimates

Important Ratios

Particulars	FY20A	FY21E	FY22E	FY23E
(A) Margins (%)				
Gross Profit Margin	72.7	71.9	72.4	72.8
EBIDTA Margin	27.3	28.9	28.5	28.6
EBIT Margin	19.1	21.1	21.1	21.7
Tax rate	13.6	23.0	22.0	22.0
Net Profit Margin	12.9	13.9	15.5	16.6
(B) As Percentage of Net Sales (%)				
COGS	27.3	28.1	27.6	27.2
Employee	18.0	18.2	17.7	17.5
Other	27.4	24.8	26.2	26.7
(C) Measure of Financial Status				
Gross Debt / Equity	0.9	0.6	0.4	0.3
Interest Coverage	3.4	4.9	8.7	16.0
Inventory days	99	90	84	82
Debtors days	76	73	64	63
Average Cost of Debt	9.8	9.3	7.2	5.4
Payable days	95	82	82	78
Working Capital days	63	70	92	125
FA T/O	1.1	1.3	1.5	1.7
(D) Measures of Investment				
AEPS (Rs)	60.5	69.1	84.4	99.6
CEPS (Rs)	99.2	108.3	124.7	140.7
DPS (Rs)	39.4	43.8	30.8	30.8
Dividend Payout (%)	65.0	63.4	36.5	30.9
BVPS (Rs)	285.0	323.3	377.0	445.8
RoANW (%)	21.5	22.7	24.1	24.2
RoACE (%)	14.8	15.7	16.8	17.6
RoAIC (%)	16.4	19.4	22.1	26.2
(E) Valuation Ratios				
CMP (Rs)	2657	2657	2657	2657
P/E	43.9	38.4	31.5	26.7
Mcap (Rs Mn)	449,611	449,611	449,611	449,611
Mcap/ Sales	5.7	5.3	4.9	4.4
EV	486,892	477,805	462,755	447,914
EV/Sales	6.1	5.7	5.0	4.4
EV/EBITDA	22.4	19.6	17.6	15.5
P/BV	9.3	8.2	7.0	6.0
Dividend Yield (%)	1.5	1.6	1.2	1.2
(F) Growth Rate (%)				
Revenue	3.5	6.0	9.7	9.8
EBITDA	9.4	12.2	8.1	10.0
EBIT	11.0	16.9	10.1	12.8
PBT	111.3	28.0	20.5	18.0
APAT	29.2	14.2	22.1	18.0
EPS	29.2	14.2	22.1	18.0

Cash Flow

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
CFO	16,172	23,985	25,590	24,012
CFI	(2,534)	(3,730)	(2,994)	(2,510)
CFF	(15,132)	(21,168)	(13,545)	(11,661)
FCFF	13,638	20,255	22,596	21,502
Opening Cash	8,160	6,667	5,753	14,804
Closing Cash	6,667	5,753	14,804	24,644

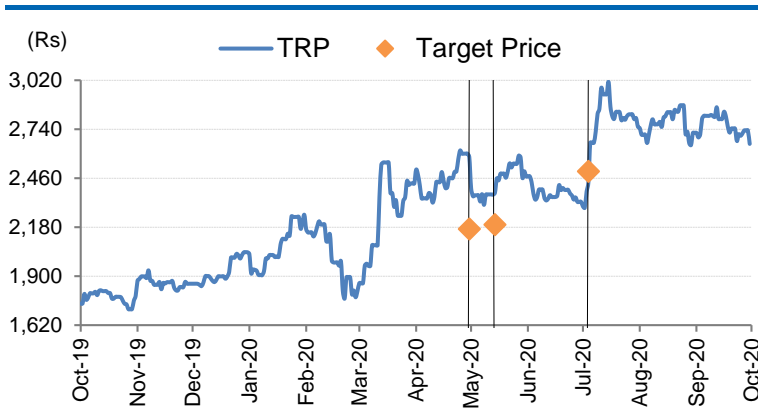
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
May-20	Sell	2,170	2,582
Jun-20	Sell	2,195	2,377
Jul-20	Reduce	2,500	2,438

*Price as on recommendation date

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