



Torrent Pharmaceuticals Limited

Healthy quarter; concerns yet to abate fully

Pharmaceuticals | Sharekhan code: TORNTPHARM | Result Update

3R MATRIX

	+	=	-
Right Sector (RS)	✓	✗	✗
Right Quality (RQ)	✓	✓	✗
Right Valuation (RV)	✓	✓	✗

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS	✓	↔	✓
RQ	✗	↔	✗
RV	✗	↔	✗

Reco/View

Reco: Hold	↔
CMP: Rs. 2,758	
Price Target: Rs. 3,100	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

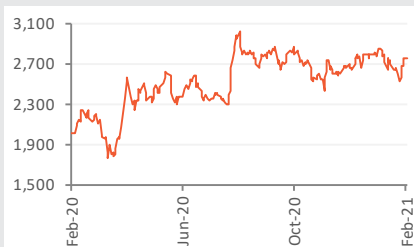
Company details

Market cap:	Rs. 46,676 cr
52-week high/low:	Rs. 3,040/1619
NSE volume: (No of shares)	5.96 lakh
BSE code:	500420
NSE code:	TORNTPHARM
Free float: (No of shares)	4.9 cr

Shareholding (%)

Promoters	71.3
FII	8.7
DII	12.3
Others	7.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.2	8.0	-6.2	36.5
Relative to Sensex	-8.5	-14.6	-41.2	11.6

Sharekhan Research, Bloomberg

Summary

- We retain Hold recommendation on Torrent Pharmaceuticals Limited (Torrent) with a revised PT of Rs 3100.
- Torrent has reported a healthy performance for the quarter, largely backed by a growth in the domestic and Europe business, while the US and the Brazil business continued to remain under pressure.
- Going ahead the outlook for the India business is healthy and the company expects to outperform the industry growth backed by price increase and new product launches. Europe business too is on the path to improvement
- Lack of new launches, price erosion, OAL/WL status at Indrad Dahej & US plant could drag the US business, while adverse currency movements to impact growth in Brazil business.

Torrent Pharmaceuticals Limited (Torrent) reported healthy performance for Q3FY2021, led by a slightly better than expected operating performance. Revenues for the quarter stood at Rs 1995 crore, up by a meager 1.5% y-o-y and were in line with the estimates. The operating margins for the quarter stood at 30.4%, up by 296 bps y-o-y, driven by savings in the other expenses. Tracking the operating performance, the PAT for the quarter stood at Rs 297 crore, up 18.3% y-o-y and was ahead of the estimated RS 276 cr. Torrent's India business has higher dependence on chronic therapies, which bodes well for the company. The company derives ~60% of its sales collectively from India and Brazil markets. Torrent has outperformed the industry growth in both these markets and looks to sustain the momentum backed by new launches. In the India business a strong new launch pipeline of ~20 new products in FY2021 and a slightly lower no of launches in FY2022, would drive the growth leading to market outperformance. Brazil though is growing in healthy double digits, an adverse impact of currency could overweigh on the performance. In local currency, Torrent looks to outperform the Brazilian market growth backed by new launches in the branded generic space. The Europe business is on the path to improvement. Growth in the US is expected to be constrained due to price erosion and the absence of new launches. Torrent has submitted responses to the USFDA for its three plants, classified as OAI/WL by the regulator. The management expects the Levittown plant to commence operations possibly by end of FY2021, while a revert from the USFDA on Dahej and Indrad is awaited. Timely and successful resolution of USFDA issues is critical from growth perspective as new product approvals could be expected once the plants get clearances.

Key positives

- The India formulations business grew by 7% for the quarter, outperforming the growth in the Indian pharmaceutical markets.
- Torrent has repaid Rs. 850 crore of debt in 9MFY2021 and has guided to repay around Rs 1000 cr in FY2021.

Key negatives

- US sales declined by 23.4% y-o-y due to the of lack of new launches and price erosion.
- Delay in resolution of OAI/WL at Indrad, Dahej and US plants.
- Brazil revenues declined by 8% y-o-y impacted by the adverse currency situation.
- Operating expenses to normalize in FY2022, hence management expects operating margins to be around 29% (for FY2022) as compared to ~30.5% in FY2021.

Our Call

Valuation - Maintain Hold with a Revised PT of 3100: Torrent has reported a healthy performance for the quarter, largely backed by a growth in the domestic and Europe business, while the US and the Brazil business continued to remain under pressure. Going ahead, the outlook for the India business is healthy and the company expects to outperform the industry growth backed by sustained price increase and new product launches. The international business is expected to be under stress, attributable to a weak performance of US business driven by lack of new launches and price erosion. The Brazil business is also witnessing pressures on account of adverse currency movement. The Europe (Germany) business is on the path to revive as the company has addressed quality related issues. Torrent's three plants – Dahej, Indrad, and Levittown are under USFDA scanner. Management sees the Levittown plant to commence operations by end of FY2021, a revert on Dahej and Indrad plants is awaited from the USFDA. A timely and successful resolution of both these plants is critical from the growth perspective. On the basis of Q3FY2021 results we have marginally increased the estimates for FY2022/FY2023. At the CMP the stock is trading at 30.9x / 26x its FY2022E / FY2023 E EPS, which has been trending towards the higher end of the long term average multiple, thus leaving limited scope for multiple expansion. Consequently, we retain Hold recommendation on the stock with a revised PT of Rs 3100.

Key risk

Delays in resolution of USFDA issues at its plants.

Valuation (Consolidated)

Particulars	FY2019	FY2020	FY2021E	FY2022E	FY2023E
Net sales	7461.0	7780.0	8284.1	9348.1	10859.3
Operating Profit	1772.0	2011.0	2526.7	2701.6	3094.9
OPM (%)	23.8	25.8	30.5	28.9	28.5
Adjusted net profit	792.0	1025.0	1308.2	1516.5	1800.5
EPS (Rs)	46.6	60.3	77.0	89.2	105.9
PER (x)	59.2	45.7	35.8	30.9	26.0
EV/Ebitda (x)	29.6	26.1	20.1	18.3	15.5
P/BV (x)	9.9	9.7	7.9	6.6	5.4
ROCE (%)	12.6	14.8	17.9	19.2	20.6
RONW (%)	16.9	21.5	24.3	23.2	22.8

Source: Company; Sharekhan estimates

Healthy performance for Q3FY2021: Torrent reported healthy performance for Q3FY2021, led by a slightly better than expected operating performance. Revenues for the quarter stood at 1995 crore, up by a meager 1.5% YoY and were in line with the estimates. The revenues from the India business grew by 7% YoY reflecting a growth in the IPM. The Brazil revenues declined by 8% YoY largely impacted by unfavorable currency movements, however in local currency terms the growth stood in double digits. The US sales continue to be impacted due to absence of new launches, impact of Price erosion, which was in high single digits. The German revenues grew by 21% YoY as the quality related issues were resolved and the business gained momentum. The operating margins for the quarter stood at 30.4%, up by 296 bps YoY and were slightly better than the estimates. The expansion in operating margins can be largely attributable to the savings in the other expenses due to lower SGA. The operating profits for the quarter stood at Rs 607 crore a growth of 12% YoY, but were in line with the estimates of Rs 597 crore. The tax rate for the quarter stood at 16.8% as compared to 21.3% in Q3FY2020. Tracking the operating performance, the PAT for the quarter stood at Rs 297 crore, up 18.3% y-o-y and was ahead of the estimated RS 276 cr.

India business to outperform the industry growth; Europe on the improvement path; US to be under stress:

Torrent's India business largely comprises the domestic formulations business, which has staged a healthy growth of 7% y-o-y to Rs 930 crore. The healthy growth in the Chronic as well sub chronic space coupled with new launches drive the growth for the quarter. The management expects the domestic market growth to outperform the industry growth backed by multiple factors which include new product launches, restructuring of the field force (with an objective to focus on high growth products) and resumption / increase in patient footfalls. Torrent has launched a strong 17 new products in YTD December 2020 while it plans to launch 4 to 5 new products in Q4FY2021 taking the total tally to 20+ new launches in FY2021. Going ahead the new launches are expected to continue in FY2022, albeit at a slower pace as compared to FY2021. The outlook for the German (Europe) business is also improving and the management expects a pick up over the next few quarters, though a meaningful growth is expected in FY2022. Brazil is also an important market for Torrent and the volumes in the market have posted a strong growth, which the management believes to sustain going ahead. However an adverse currency movement (depreciation of the Brazillian real) is expected to over weigh on the growth in the near to medium term at-least. Torrent's US business too is under stress on the back of lack of new launches, adverse impact of price erosion in US generics. Also the USFDA clearance for Dahej and Indrad plant is awaited, which would also slow down the growth of the US business.

CAPA at Indrad and Dahej plants done; USFDA response awaited: Torrent's Dahej plant, inspected by the USFDA (between March 11-19, 2019) was classified as OAI. The management has mentioned that it has completed its corrective and preventive actions (CAPA) around the areas highlighted by the USFDA and has submitted its responses. A reply from the USFDA is awaited on this. Moreover, the US manufacturing plant located at Levittown (Pennsylvania) was also issued a warning letter for cGMP violations relating to finished pharmaceutical products and management expects to start production of at the plant towards the end of FY2021 or early FY2022. Torrent's sizeable fillings for the US markets are linked to Dahej and Indrad plants. Moreover, as these are yet to be cleared by the USFDA, new product approvals are on hold. The company has submitted its responses to the regulator and is awaiting a revert.

Q3FY2021 Conference call highlights:

Geographical revenue mix

- ◆ Torrent's domestic revenue grew by 7% y-o-y for the quarter to Rs 930 crore. The company has outperformed the industry's growth because of its chronic heavy portfolio and the management is confident of sustaining

the outperformance. Also the company has plans to launch around 20+ products in the FY2021 in the India markets (in the similar therapy areas it is present in Now), while it sees the momentum slowing down in FY2022.

- ◆ Revenue from the US declined by 23.4% y-o-y to Rs 292 crore, impacted by price erosion in the base business and absence of new product launches.
- ◆ Revenue from Brazil at Rs. 173 crore declined by 8.5% y-o-y for the quarter. However, local currency sales increased in double digits. Torrent has outperformed the industry and expects to continue outperforming the industry backed by new launches. In the branded generic space Torrent looks to launch 3 to 5 new products in FY2022.
- ◆ Europe (Germany) sales bucked the trend and grew by 21% YoY to RS 265 cr, the second consecutive quarter of a growth after 4 consecutive quarters of decline. The company has largely completed the upgradation of its quality management systems. The revenue traction is expected to improve going ahead.

ANDA approvals (US markets): As of Q3FY2021, the company has 47 ANDAs pending for approvals and the company received six tentative approvals.

Debt repayment: In 9MFY2021, the company has repaid around Rs. 850 crore debt and management expects to achieve its debt repayment target of around 1000 cr in FY2021.

Results (Consolidated)

Particulars	Rs cr				
	Q3FY2021	Q3FY2020	YoY %	Q2FY2021	QoQ %
Total Sales	1,995.0	1,966.0	1.5	2,017.0	-1.1
Operating profit	607.0	540.0	12.4	635.0	-4.4
Other income	8.0	53.0	-84.9	6.0	33.3
EBITDA	615.0	593.0	3.7	641.0	-4.1
Interest	91.0	111.0	-18.0	92.0	-1.1
Depreciation	167.0	163.0	2.5	165.0	1.2
PBT	357.0	319.0	11.9	384.0	-7.0
Taxes	60.0	68.0	-11.8	74.0	-18.9
Adjusted PAT	297.0	251.0	18.3	310.0	-4.2
Margins			BPS		BPS
OPM %	30.4	27.5	296	31.5	-106

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Growth momentum to improve

Indian pharmaceutical companies are better placed to harness opportunities and report healthy growth going ahead. Indian companies are among the most competitive ones globally and hold a sizeable market share in most developed as well as other markets. Moreover, other factors such as easing of pricing pressures (especially in the US generics market), rise in product approvals, and plant resolutions by the USFDA coupled with strong growth prospects in domestic markets and emerging opportunities in the API space would be key growth drivers. This would be complemented by strong capabilities developed by Indian companies (leading to a shift towards complex molecules and biosimilars) and commissioning of expanded capacities by select players over the medium term. Collectively, this indicates a strong growth potential going ahead for pharma companies.

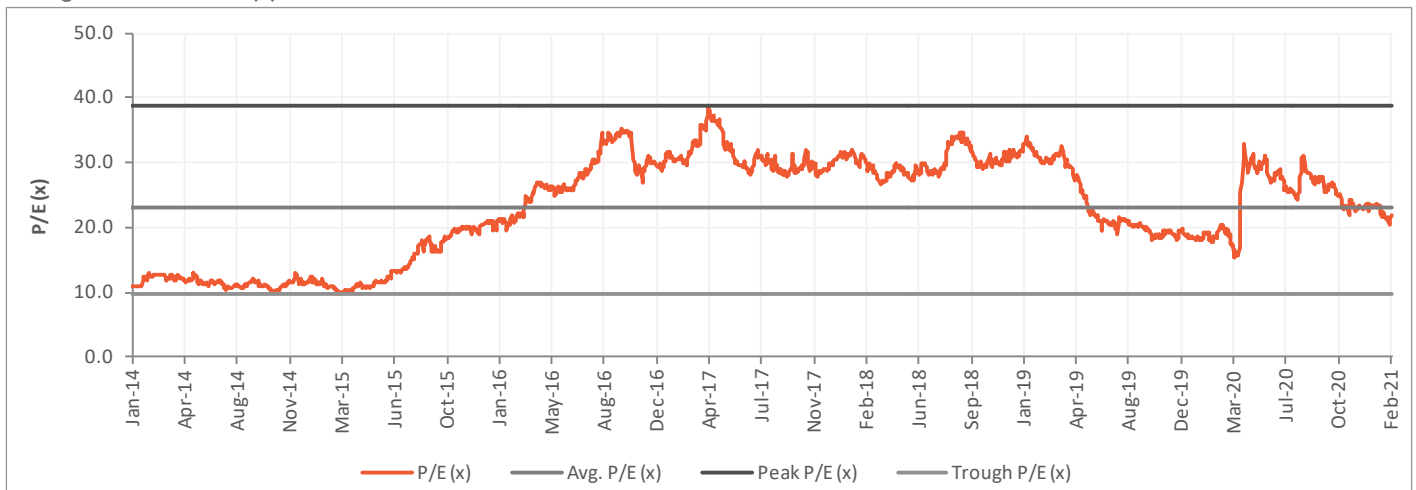
■ Company Outlook – Concerns yet to wane

Torrent is a leading pharma company present in emerging as well as developed markets. The company has a higher exposure to chronic therapies. Moreover, the company derives a substantial portion of its sales from India followed by US, Germany, and Brazil. The company has been outperforming in the Indian as well as Brazilian markets and management expects to sustain the traction going ahead as well. However the adverse currency situation in Brazil is expected to over-weigh on the performance of the company. The performance in the Europe is also getting on the improvement path albeit a meaningful revival is likely in FY2022. The US business of the company has been under pressure as three of its plants, which cater to US markets – Dahej, Indrad, and Levittown (US) are under the USFDA scanner with OAI/WL classification. Torrent has submitted its responses to the regulator and is awaiting a response from USFDA on this. Torrent expects the Levittown plant to commence operations by the end of FY2021. A timely and successful resolution of these issues is critical from the company's growth perspective as new product approvals are held up, while price erosion is impacting the base business.

■ Valuation – Maintain Hold with a Revised PT of 3100

Torrent has reported a healthy performance for the quarter, largely backed by a growth in the domestic and Europe business, while the US and the Brazil business continued to remain under pressure. Going ahead, the outlook for the India business is healthy and the company expects to outperform the industry growth backed by sustained price increase and new product launches. The international business is expected to be under stress, attributable to a weak performance of US business driven lack of new launches and price erosion. The Brazil business is also witnessing pressures on account of adverse currency situation. The Europe (Germany) business is on the path to revive as the company has addressed quality related issues. Torrent's three plants – Dahej, Indrad, and Levittown are under USFDA scanner. Management sees the Levittown plant to commence operations by end of FY2021, a revert on Dahej and Indrad plants is awaited from the USFDA. A timely and successful resolution of both these plants is critical from the growth perspective. On the basis of Q3FY2021 results we have marginally increased the estimates for FY2022/FY2023. At the CMP the stock is trading at 30.9x / 26x its FY2022E / FY2023E EPS, which has been trending towards the higher end of the long term average multiple, thus leaving limited scope for multiple expansion. Consequently, we retain Hold recommendation on the stock with a revised PT of Rs 3100.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)			EV/EBIDTA (x)			RoE (%)		
				FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E
Torrent Pharma	2758	16.99	46676	45.7	35.8	30.9	26.1	20.1	18.3	21.5	24.3	23.2
Lupin	1070	45.3	48,519	137.5	44.8	26.3	22.9	17.6	12.1	2.8	8.0	11.9
Cipla	848	80.6	68352	44.2	27.1	23.5	22.1	15.8	13.8	10.1	13.9	14.6

Source: Company, Sharekhan estimates

About company

Torrent, the flagship company of Torrent Group, was incorporated in 1972. Torrent has a strong international presence across 40 countries with operations in regulated and emerging markets such as the US, Europe, Brazil, and the Rest of the World. The company operates through its wholly owned subsidiaries spread across 12 nations with major setups in Brazil, Germany, and US. 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 a significant presence in gastro-intestinal, diabetology, anti-infective, and pain management segments.

Investment theme

Torrent continues to focus on a branded business mix from India and Brazil, which balances well for sustainable growth in a challenging global environment for the pharma sector. US business is also stable. Operating leverage from the acquired domestic business is likely to be visible from FY2020. Three manufacturing plants of Torrent are reeling under regulatory issues with a warning letter being issued by the USFDA. Management expects at least 12-15 months for the issues to be resolved; and till such time, approvals from these plants would be withheld. Torrent has submitted its responses to the regulator and is awaiting a revert on this. Timely and successful resolution of the USFDA issues is critical from the growth perspective.

Key Risks

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

Additional Data

Key management personnel

Mr. Sudhir Mehta	Chairman (Emeritus)
Mr. Samir Mehta	Executive Chairman
Mr. Sudhir Menon	CFO
Dr. Chaitanya Dutt	Director (R&D)

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	FMR LLC	1.53
2	UTI Asset Management Co Ltd	1.27
3	HDFC Asset Management	1.05
4	HDFC Life Insurance Co Ltd	1.00
5	Axis Asset Management Co Ltd/India	0.99
6	Mirae Asset Global investment Company	0.93
7	Vanguard Group Inc	0.89
8	T Rowe Price Group Inc	0.8
9	Blackrock Inc	0.75
10	Reliance Capital Trustee Co Ltd	0.6

Source: Bloomberg

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Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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