

BUY

Q4 miss on top-line, sustained margins and specialty to drive growth

Sun missed our estimate on the top-line with sales in Q4 at Rs84bn (up 4% YoY) primarily due to lower US sales at US\$370mn (down US\$5mn QoQ). India growth was robust at 13% YoY. Controlled spend aided EBITDA margins at 24.2%. Debt reduction of \$580mn in FY21 led to lower interest outgo. One-time provision of US\$80mn (w.r.t Taro's anti-trust cases in the US), led to recognition of higher deferred tax. Adjusting for the one-off, PAT came in at Rs14.5bn (we saw Rs14.2bn). Management refrained from any guidance for FY22E citing COVID related uncertainties; Q1 to witness high growth led by India sales and lower SGA expenses (aided by COVID). With current US generic portfolio not firing, Sun announced its plans to enter US biosimilar segment. Sketchy details indicate that Sun might look for partners, in-licensing strategy to enter this segment. Nonetheless, launches are scheduled in FY28/30.

Key triggers: (1) Ilumya/Cequa growth to outweigh Absorica's generic risk, (2) Taro seems to have bottomed in terms of operating performance, lower COVID cases likely to drive Taro's earnings efficiency, (3) Domestic business to sustain its leadership position with healthy growth post field force expansion, (4) USFDA resolution of Halol (currently under OAI)

Key risk: High R&D (~9% of sales) & marketing expenses on US specialty to keep margins under check.

Outlook and Valuation: As Rx trends & MS gain traction, we believe specialty revenue momentum should sustain, despite Absorica facing generic competition. We expect Ilumya to achieve US sales of US\$200mn by FY23E and gain favorable reimbursement status. Sun's investment of US\$1bn in building its specialty portfolio, is in the last leg of its specialty investment cycle. We expect its specialty portfolio to achieve profitability in FY23E with gross margin expansion and the end of negative operating leverage post breakeven in specialty assets expected to aid EBITDA margin expansion of ~390 bps over FY20-23. Sun's valuation, at 22.6x FY23E earnings, does not justify its visibility for specialty-business-driven growth and steady outlook on its India and ROW formulations, in our view. Risk reward is favorable given the strong FCF generation over FY20-23E and OCF/EBITDA at ~77%. Our SOTP based TP of Rs786 values Sun at 25x FY23E.

Q4FY21 Result (Rs Mn)

Particulars	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)
Revenue	85,230	81,849	4.1	88,368	(3.6)
Total Expense	64,638	66,799	(3.2)	65,023	(0.6)
EBITDA	20,592	15,051	36.8	23,345	(11.8)
Depreciation	5,535	5,754	(3.8)	5,319	4.1
EBIT	15,057	9,297	62.0	18,026	(16.5)
Other Income	1,110	1,022	8.6	3,150	(64.8)
Interest	301	518	(41.9)	261	15.3
EBT	9,030	5,774	56.4	21,631	(58.3)
Tax	550	831	(33.8)	2,449	(77.5)
RPAT	8,942	3,998	123.6	18,525	(51.7)
APAT	14,565	8,026	81.5	17,809	(18.2)
			(bps)		(bps)
Gross Margin (%)	73.7	71.8	187	73.6	11
EBITDA Margin (%)	24.2	18.4	577	26.4	(226)
NPM (%)	10.5	4.9	561	21.0	(1047)
Tax Rate (%)	6.1	14.4	(829)	11.3	(523)
EBIT Margin (%)	17.7	11.4	631	20.4	(273)

CMP	Rs 700
Target / Upside	Rs 786 / 12%
NIFTY	15,338

Script Details

Equity / FV	Rs 2,399mn / Rs 1
Market Cap	Rs 1,678bn
	USD 23bn
52-week High/Low	Rs 722/ 445
Avg. Volume (no)	7,396,270
Bloom Code	SUNP IN

Price Performance	1M	3M	12M
Absolute (%)	9	18	52
Rel to NIFTY (%)	6	13	(7)

Shareholding Pattern

	Sep'20	Dec'20	Mar'21
Promoters	54.7	54.7	54.5
MF/Banks/FIs	27.4	28.0	11.9
FIIIs	12.7	12.4	11.7
Public / Others	5.1	5.0	12.2

Valuation (x)

	FY21E	FY22E	FY23E
P/E	27.9	24.6	22.6
EV/EBITDA	19.1	17.4	15.5
ROE (%)	6.3	14.0	13.8
RoACE (%)	11.8	11.2	11.5

Estimates (Rs mn)

	FY21E	FY22E	FY23E
Revenue	334,981	367,778	396,625
EBITDA	84,677	90,988	99,577
PAT	60,087	68,283	74,235
EPS (Rs.)	25.0	28.5	30.9

VP - Research: Sapna Jhawar
Tel: +9122 40969724
E-mail: sapnaj@dolatcapital.com

Associate: Zain Gulam Hussain
Tel: +9122 40969725
E-mail: zain@dolatcapital.com

Exhibit 1: Dismal base generic performance to be offset by specialty

(US\$ mn)	FY17	FY18	FY19	FY20	FY21
Total US sales	2,051	1,360	1,547	1,488	1,359
Taro	785	549	537	496	423
US Specialty	309	346	339	387	414
Base generic	957	465	670	605	522

Source: Company, DART

Exhibit 2: Revenue Mix

(Rs mn)	Q4FY20	Q4FY21	YoY (%)	Q3FY21	QoQ (%)	FY21	FY20	YoY (%)
US	27,129	26,946	(0.7)	27,609	(2.4)	1,00,839	1,05,425	(4.4)
India	23,648	26,709	12.9	27,528	(3.0)	1,03,432	97,102	6.5
ROW	11,212	11,913	6.3	12,758	(6.6)	48,191	45,210	6.6
Emerging Markets	13,540	14,015	3.5	15,071	(7.0)	57,834	55,044	5.1
API	4,834	4,357	(9.9)	4,505	(3.3)	19,504	19,159	1.8
Others	417	374	(10.3)	348	7.7	1,593	1,312	21.4
Total revenues	80,780	84,314	4.4	87,818	(4.0)	3,31,392	3,23,252	2.5

Source: Company, DART

Key Concall takeaways

- **Operational performance:** Sun reported 24.2% EBITDA margins in 4Q despite weak top-line due to lower sales at Taro. Higher US specialty and India sales aided EBITDA. Sun guided that tailwind of business savings (lower marketing costs) could continue in 1Q and would normalize gradually. Digital transformation could add structural benefits to the company.
- **Global specialty sales** in 4Q was US\$139mn (down 6% QoQ) impacted by higher channel inventory in 3Q and lower clinic footfalls. In FY21, global specialty portfolio grew 10% YoY at US\$473mn with Ilumya grew 50% YoY at US\$143mn in FY21. Similarly, Cequa surpassed its pre-COVID peak, led by steady expansion of the US market, despite new competition. Levulan is yet to pick up as visit to dermatologists remain impacted. R&D spend towards specialty was 23% of total R&D spend.
 - a. **Ilumya:** Ilumya, Sun's flagship specialty product, up 50% YoY at US\$143mn. Sun plans to bolster its marketing initiatives for Ilumya by utilizing the recently released five-year sustained efficacy and safety data of the brand. Despite multiple challenges and a delayed entry, Ilumya continue to gain traction on better dosing regimen (less frequent maintenance doses, hence cost effective) and formulary coverage. Trial for psoriatic arthritis was impacted due to COVID, company intends to start patient recruitment in new sites within next few weeks.
 - b. **Cequa:** Per the management, product is well accepted within doctor community and management remains confident of achieving market share gains.
 - c. **Absorica:** Patent to expire in Sep'21, competition (Teva and Mylan) entered market in Apr'21. Sun's effort to shift patients on Absorica to the Absorica LD (low dose) form before the generic entry for Absorica was hampered by COVID-19 and it has transferred ~25% of patients to the LD form. Despite the expected imminent entry of competing generics for Cequa and Absorica, Sun remains confident about the reasonable market uptake of its brands on the back of notable offerings in terms efficacy, safety and durability of results.

- **US:** Ex-specialty business and Taro, the generic business has de-grown over the last 3-4 years in the absence of big ticket launch. The company reiterated that generic market continues to remain competitive led by price erosion. Sun is waiting for USFDA's move on compliance status for Halol. It launched 18 products in FY21 and guided for 2-3 launches per quarter. Sun has 501 approved products and 94 pending approval in the US.
- **Taro:** Taro reported sales of US\$148mn in 4Q, flat QoQ. Due to one-time provision of US\$80mn for anti-trust civil litigation in the US, it reported loss in 4Q. Taro's margins have declined visibly from peak of 60% in FY17 to 26% in FY21. Further, with derma facing lower Rx generation due to COVID (clinics shutdown) intensified the pressure. With COVID cases declining and increase in patient footfalls, Taro is likely to witness improvement in its operating performance.
- **R&D spend:** The R&D spend for the quarter stood at 6.4% of sales at Rs5.5bn. Of this, the specialty R&D was at 23%. Sun indicated that while R&D will scale up to 8-9% over the next 2-3 years, mix within R&D will be inclined towards specialty.
- **India formulations:** Domestic formulations grew 13% YoY in 4Q, led by continued growth momentum in chronic (double digit growth), recovery in sub-chronic and moderation in decline in acute segment. For FY21, domestic formulations grew 6.5% YoY. With 95% MRs back on the field, large part of the expenditure is back. Sun has completed its field force expansion and expects to improve reach and drive higher growth over the medium term. Sun launched 30 new products in FY21 through its digital platform and indicated that this route could add to some structural savings in the business.

Other branded markets: Emerging markets grew 5% YoY led by tender business in South Africa. RoW markets grew 7% YoY in FY21. The API business was subdued with 2% YoY growth in FY21.

Profit and Loss Account

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Revenue	328,375	334,981	367,778	396,625
Total Expense	258,634	250,304	276,790	297,048
COGS	92,305	86,901	98,331	104,677
Employees Cost	63,624	68,622	72,909	78,711
Other expenses	102,706	94,781	105,550	113,660
EBIDTA	69,742	84,677	90,988	99,577
Depreciation	20,528	20,800	22,771	23,844
EBIT	49,214	63,878	68,217	75,732
Interest	3,027	1,414	1,270	1,146
Other Income	6,360	8,355	8,609	8,812
Exc. / E.O. items	(2,450)	(42,825)	0	0
EBT	50,096	27,994	75,555	83,398
Tax	8,228	5,147	12,844	14,178
RPAT	37,649	29,038	68,283	74,235
Minority Interest	4,070	(6,315)	(5,683)	(5,115)
Profit/Loss share of associates	(148)	(123)	(111)	(100)
APAT	40,064	60,087	68,283	74,235

Balance Sheet

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Sources of Funds				
Equity Capital	2,399	2,399	2,399	2,399
Minority Interest	38,602	30,170	30,170	30,170
Reserves & Surplus	450,245	462,229	509,863	561,470
Net Worth	452,645	464,628	512,262	563,869
Total Debt	75,783	33,430	31,759	30,171
Net Deferred Tax Liability	21,873	21,694	14,661	7,534
Total Capital Employed	588,903	549,922	588,852	631,745

Applications of Funds

Net Block	163,655	152,653	150,443	141,004
CWIP	77,018	78,545	79,545	80,545
Investments	58,658	70,191	70,191	70,191
Current Assets, Loans & Advances	351,441	339,714	378,954	431,264
Inventories	78,750	89,970	93,711	97,538
Receivables	94,212	90,614	91,886	94,885
Cash and Bank Balances	64,875	64,455	95,211	136,034
Loans and Advances	45,676	44,612	46,207	48,806
Other Current Assets	18,953	18,762	20,638	22,701
Less: Current Liabilities & Provisions	61,869	91,181	90,280	91,259
Payables	40,937	39,737	40,549	43,104
Other Current Liabilities	20,931	51,444	49,731	48,155
<i>sub total</i>				
Net Current Assets	289,572	248,533	288,673	340,005
Total Assets	588,903	549,922	588,852	631,745

E – Estimates

Important Ratios

Particulars	FY20A	FY21E	FY22E	FY23E
(A) Margins (%)				
Gross Profit Margin	71.9	74.1	73.3	73.6
EBIDTA Margin	21.2	25.3	24.7	25.1
EBIT Margin	15.0	19.1	18.5	19.1
Tax rate	16.4	18.4	17.0	17.0
Net Profit Margin	11.5	8.7	18.6	18.7
(B) As Percentage of Net Sales (%)				
COGS	28.1	25.9	26.7	26.4
Employee	19.4	20.5	19.8	19.8
Other	31.3	28.3	28.7	28.7
(C) Measure of Financial Status				
Gross Debt / Equity	0.2	0.1	0.1	0.1
Interest Coverage	16.3	45.2	53.7	66.1
Inventory days	88	98	93	90
Debtors days	105	99	91	87
Average Cost of Debt	3.5	2.6	3.9	3.7
Payable days	46	43	40	40
Working Capital days	322	271	286	313
FA T/O	2.0	2.2	2.4	2.8
(D) Measures of Investment				
AEPS (Rs)	16.7	25.0	28.5	30.9
CEPS (Rs)	25.3	33.7	38.0	40.9
DPS (Rs)	5.7	7.5	8.3	9.1
Dividend Payout (%)	34.4	29.9	29.0	29.3
BVPS (Rs)	188.7	193.7	213.5	235.0
RoANW (%)	8.7	6.3	14.0	13.8
RoACE (%)	8.2	11.8	11.2	11.5
RoAIC (%)	9.7	12.7	13.9	15.3
(E) Valuation Ratios				
CMP (Rs)	700	700	700	700
P/E	41.9	27.9	24.6	22.6
Mcap (Rs Mn)	1,678,310	1,678,310	1,678,310	1,678,310
Mcap/ Sales	5.1	5.0	4.6	4.2
EV	1,640,244	1,615,985	1,583,557	1,541,147
EV/Sales	5.0	4.8	4.3	3.9
EV/EBITDA	23.5	19.1	17.4	15.5
P/BV	3.7	3.6	3.3	3.0
Dividend Yield (%)	0.8	1.1	1.2	1.3
(F) Growth Rate (%)				
Revenue	13.0	2.0	9.8	7.8
EBITDA	9.0	21.4	7.5	9.4
EBIT	5.9	29.8	6.8	11.0
PBT	31.5	(44.1)	169.9	10.4
APAT	8.2	50.0	13.6	8.7
EPS	8.2	50.0	13.6	8.7

Cash Flow

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
CFO	65,324	67,503	77,340	76,479
CFI	(46,990)	(7,123)	(21,561)	(15,405)
CFF	(26,214)	(60,801)	(25,023)	(20,251)
FCFF	18,334	60,380	55,780	61,073
Opening Cash	72,756	64,875	64,455	95,211
Closing Cash	64,875	64,455	95,211	136,034

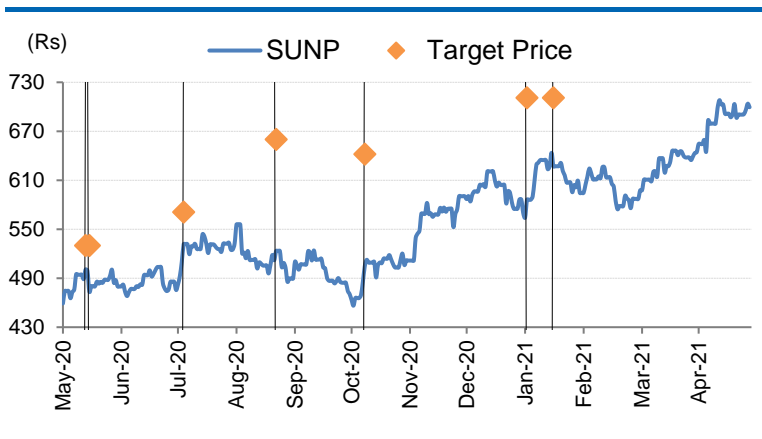
E – Estimates

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.)
Jun-20	Buy	530	501
Jun-20	Buy	530	474
Jul-20	Buy	571	532
Sep-20	Buy	660	523
Nov-20	Buy	642	505
Jan-21	Buy	711	586
Feb-21	Buy	711	627

*Price as on recommendation date

DART Team

Purvag Shah	Managing Director	purvag@dolatcapital.com	+9122 4096 9747
--------------------	--------------------------	--------------------------------	------------------------

Amit Khurana, CFA	Head of Equities	amit@dolatcapital.com	+9122 4096 9745
--------------------------	-------------------------	------------------------------	------------------------

CONTACT DETAILS

Equity Sales	Designation	E-mail	Direct Lines
Dinesh Bajaj	VP - Equity Sales	dineshb@dolatcapital.com	+9122 4096 9709
Kapil Yadav	VP - Equity Sales	kapil@dolatcapital.com	+9122 4096 9735
Yomika Agarwal	VP - Equity Sales	yomika@dolatcapital.com	+9122 4096 9772
Jubbin Shah	VP - Equity Sales	jubbins@dolatcapital.com	+9122 4096 9779
Ashwani Kandoi	AVP - Equity Sales	ashwanik@dolatcapital.com	+9122 4096 9725
Lekha Nahar	AVP - Equity Sales	lekhan@dolatcapital.com	+9122 4096 9740
Equity Trading	Designation	E-mail	
P. Sridhar	SVP and Head of Sales Trading	sridhar@dolatcapital.com	+9122 4096 9728
Chandrakant Ware	VP - Sales Trading	chandrakant@dolatcapital.com	+9122 4096 9707
Shirish Thakkar	VP - Head Domestic Derivatives Sales Trading	shirisht@dolatcapital.com	+9122 4096 9702
Kartik Mehta	Asia Head Derivatives	kartikm@dolatcapital.com	+9122 4096 9715
Dinesh Mehta	Co- Head Asia Derivatives	dinesh.mehta@dolatcapital.com	+9122 4096 9765
Bhavin Mehta	VP - Derivatives Strategist	bhavinm@dolatcapital.com	+9122 4096 9705

Dolat Capital Market Private Limited.

Sunshine Tower, 28th Floor, Senapati Bapat Marg, Dadar (West), Mumbai 400013

Analyst(s) Certification

The research analyst(s), with respect to each issuer and its securities covered by them in this research report, certify that: All of the views expressed in this research report accurately reflect his or her or their personal views about all of the issuers and their securities; and No part of his or her or their compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

I. Analyst(s) and Associate (S) holding in the Stock(s): (Nil)**II. Disclaimer:**

This research report has been prepared by Dolat Capital Market Private Limited. to provide information about the company(ies) and sector(s), if any, covered in the report and may be distributed by it and/or its affiliated company(ies) solely for the purpose of information of the select recipient of this report. This report and/or any part thereof, may not be duplicated in any form and/or reproduced or redistributed without the prior written consent of Dolat Capital Market Private Limited. This report has been prepared independent of the companies covered herein. Dolat Capital Market Private Limited. and its affiliated companies are part of a multi-service, integrated investment banking, brokerage and financing group. Dolat Capital Market Private Limited. and/or its affiliated company(ies) might have provided or may provide services in respect of managing offerings of securities, corporate finance, investment banking, mergers & acquisitions, financing or any other advisory services to the company(ies) covered herein. Dolat Capital Market Private Limited. and/or its affiliated company(ies) might have received or may receive compensation from the company(ies) mentioned in this report for rendering any of the above services. Research analysts and sales persons of Dolat Capital Market Private Limited. may provide important inputs to its affiliated company(ies) associated with it. While reasonable care has been taken in the preparation of this report, it does not purport to be a complete description of the securities, markets or developments referred to herein, and Dolat Capital Market Private Limited. does not warrant its accuracy or completeness. Dolat Capital Market Private Limited. may not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. This report is provided for information only and is not an investment advice and must not alone be taken as the basis for an investment decision. The investment discussed or views expressed herein may not be suitable for all investors. The user assumes the entire risk of any use made of this information. The information contained herein may be changed without notice and Dolat Capital Market Private Limited. reserves the right to make modifications and alterations to this statement as they may deem fit from time to time. Dolat Capital Market Private Limited. and its affiliated company(ies), their directors and employees may; (a) from time to time, have a long or short position in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions. This report is neither an offer nor solicitation of an offer to buy and/or sell any securities mentioned herein and/or not an official confirmation of any transaction. This report is not directed or intended for distribution to, or use by any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject Dolat Capital Market Private Limited. and/or its affiliated company(ies) to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to a certain category of investors. Persons in whose possession this report may come, are required to inform themselves of and to observe such restrictions.

For U.S. Entity/ persons only: "This Report is considered independent third-party research and was prepared by Dolat Capital Market Private Limited, with headquarters in India. The distribution of this Research is provided pursuant to the exemption under Rule 15a-6(a) (2) and is only intended for an audience of Major U.S. Institutional Investors (MUSIIs) as defined by Rule 15a-6(b)(4). This research is not a product of StoneX Financial Inc. Dolat Capital Market Private Limited has sole control over the contents of this research report. StoneX Financial Inc. does not exercise any control over the contents of, or the views expressed in, any research reports prepared by Dolat Capital Market Private Limited and under Rule 15a-6(a) (3), any U.S. recipient of this research report wishing to affect any transaction to buy or sell securities or related financial instruments based on the information provided in this research report should do so only through StoneX Financial Inc. Please contact Paul Karrlsson-Willis at +1 (407) 741-5310 or email Paul.Karrlsson-Willis@stonex.com and/or Igor Chernomorskiy at +1 (212)379-5463 or email Igor.Chernomorskiy@stonex.com. Under no circumstances should any U.S. recipient of this research report effect any transaction to buy or sell securities or related financial instruments through the Dolat Capital Market Private Limited."



Dolat Capital Market Private Limited.

Corporate Identity Number: U65990DD1993PTC009797

Member: BSE Limited and National Stock Exchange of India Limited.

SEBI Registration No: BSE – INZ000274132, NSE - INZ000274132, Research: INH000000685

Registered office: Office No. 141, Centre Point, Somnath, Daman – 396 210, Daman & Diu

Board: +9122 40969700 | Fax: +9122 22651278 | Email: research@dolatcapital.com | www.dolatresearch.com
