

31 October 2020

Suven Pharmaceuticals

*Lumpy quarter, prospects unchanged; retaining a Buy*Rating: **Buy**

Target Price: Rs375

Share Price: Rs314

Suven's Q2 FY21 results belied expectations. The CDMO pharma division's tepid performance pulled sales down 13% y/y (flat q/q) to Rs2.4bn. The gross margin, though, expanded 235bps to 69%. Higher overheads and employee costs compressed the EBITDA margin 450bps to 41%. Lower other income further triggered a 20.3% fall in PAT to Rs741m. The company has maintained its guidance of 15-20% FY21 PAT growth. It expects H2 FY21 growth to be driven by more order inflows, commercialisation of a new specialty chemicals product, the launch of two formulations products and a scale-up of one product in CDMO pharma. To factor in the lower profit share from its JV and the higher depreciation cost, we cut our FY21e/FY22e/FY23e PAT 3.8%/3.6%/3.6% and expect 17.9%/17.7% growth in sales/earnings over FY20-23. We retain our Buy recommendation with a lower target of Rs375 (earlier Rs380).

Specialty chemicals segment to grow faster. In Q2 FY21, the CDMO pharma division dropped 30.3% y/y to Rs1.4bn. The Covid-19 outbreak had halted orders, now expected to spill over to H2 FY21. Sales in specialty CRAMS grew 25.6% to Rs682m. Management is confident of adding one specialty chemical molecule each in H2 FY21/FY22/FY23. We expect 13.6%/17.1% CAGRs in CDMO pharma/specialty chemicals over FY20-23.

Formulations commercialisation plan on track. Sales of formulations and other services generated Rs250m in Q2 FY21. The company has so far launched three ANDAs and plans to add two in H2 FY21 and 3-4 products in FY21. We expect this segment to grow 37.8% over FY20-23.

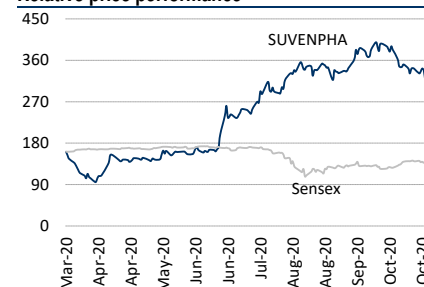
Valuation. At the CMP of Rs314, the stock quotes at 22.1x, 18.3x and 15.5x respective FY21e/22e/23e earnings. We retain our Buy recommendation, with a lower target of Rs375 (earlier Rs380), based on 18x FY23e EPS. **Risks:** Currency fluctuations, delay in new orders from clients.

Key data	SUVENPHA IN
52-week high / low	Rs420 / 87
Sensex / Nifty	39614 / 11642
3-m average volume	\$3.3m
Market cap	Rs80bn / \$1078.9m
Shares outstanding	255m

Shareholding pattern (%)	Sept'20	June'20	Mar '20
Promoters	60.0	60.0	60.0
- of which, Pledged	-	-	-
Free float	40.0	40.0	40.0
- Foreign institutions	4.2	3.6	4.2
- Domestic institutions	5.0	4.6	4.0
- Public	30.9	31.8	31.8

Estimates revision (%)	FY21e	FY22e	FY23e
Sales	1.1	1.1	1.4
EBITDA	3.3	3.8	4.3
EPS	-3.8	-3.6	-3.6

Relative price performance



Source: Bloomberg

Key financials (YE Mar)	FY19	FY20	FY21e	FY22e	FY23e
Sales (Rs m)	6,536	8,338	9,621	11,440	13,665
Net profit (Rs m)	1,879	3,170	3,618	4,372	5,175
EPS (Rs)	14.8	24.9	14.2	17.2	20.3
PE (x)	21.3	12.6	22.1	18.3	15.5
EV / EBITDA (x)	29.5	21.2	17.8	14.7	11.9
PBV (x)	13.6	9.5	7.1	5.5	4.3
RoE (%)	27.7	44.2	36.8	34.0	31.4
RoCE (%)	24.9	33.7	29.3	29.3	28.4
Dividend yield (%)	0.5	1.6	0.9	-	-
Net debt / equity (x)	0.1	0.2	0.0	(0.0)	(0.2)

Source: Company, Anand Rath Research

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Quick Glance – Consolidated Financials and Valuations

Fig 1 – Income statement (Rs m)

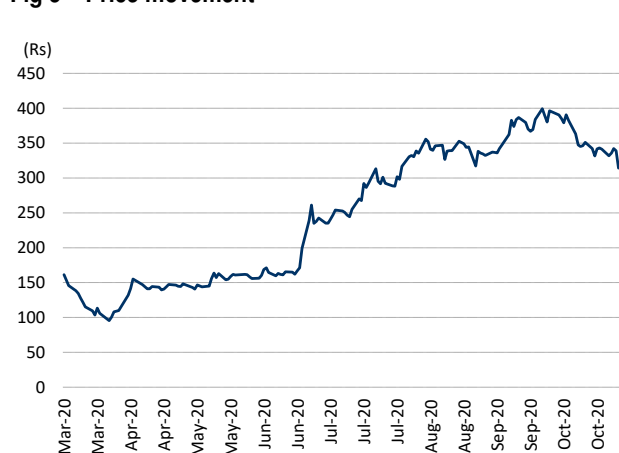
Year-end: Mar	FY19	FY20	FY21e	FY22e	FY23e
Net revenues	6,536	8,338	9,621	11,440	13,665
Growth (%)	4.5	27.6	15.4	18.9	19.5
Direct costs	1,735	2,292	2,626	3,146	3,758
SG&A	2,062	2,198	2,473	2,894	3,416
EBITDA	2,739	3,848	4,522	5,399	6,491
EBITDA margins (%)	41.9	46.1	47.0	47.2	47.5
- Depreciation	221	235	279	395	511
Other income	242	181	199	249	280
Interest expenses	38	231	115	-	-
PBT	-	482	434	499	549
Effective tax rate (%)	2,722	4,045	4,760	5,752	6,809
+ Associates / (Minorities)	31.0	21.6	24.0	24.0	24.0
Net income	1,036	3,170	3,618	4,372	5,175
Adjusted income	1,879	3,170	3,618	4,372	5,175
WANS	127	127	255	255	255
FDEPS (Rs / sh)	14.8	24.9	14.2	17.2	20.3
R&D (% of sales)	-	2	2	2	2

Fig 3 – Cash-flow statement (Rs m)

Year-end: Mar	FY19	FY20	FY21e	FY22e	FY23e
PBT	2,722	4,045	4,760	5,752	6,809
+ Non-cash items	221	235	279	395	511
Oper. prof. before WC	2,944	4,280	5,040	6,148	7,320
- Incr. / (decr.) in WC	1,161	(533)	577	551	214
Others incl. taxes	586	888	1,142	1,381	1,634
Operating cash-flow	1,198	3,925	3,320	4,216	5,472
- Capex (tang.+ intang.)	716	1,000	1,500	2,000	2,000
Free cash-flow	481	2,925	1,820	2,216	3,472
Acquisitions	-	-	-	-	-
- Div. (incl. buyback & taxes)	249	763	871	1,052	1,246
+ Equity raised	-	-	127	-	-
+ Debt raised	497	1,025	(913)	(950)	-
- Fin investments	(2,717)	3,310	-	-	-
- Misc. (CFI + CFF)	1,913	(135)	127	-	0
Net cash-flow	1,533	12	37	213	2,226

Source: Company, Anand Rathi Research

Fig 5 – Price movement



Source: Bloomberg

Fig 2 – Balance sheet (Rs m)

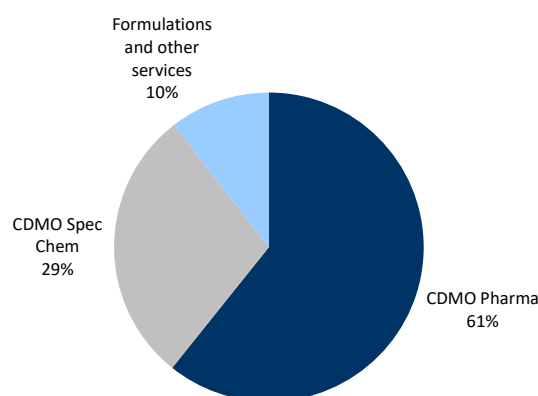
Year-end: Mar	FY19	FY20	FY21e	FY22e	FY23e
Share capital	127	127	255	255	255
Net worth	5,903	8,448	11,194	14,514	18,443
Debt	837	1,862	950	-	-
Minority interest	-	-	-	-	-
DTL / (Assets)	292	276	276	276	276
Capital employed	7,032	10,586	12,420	14,790	18,719
Net tangible assets	2,682	3,539	5,000	7,139	9,165
Net intangible assets	27	28	38	53	67
Goodwill	-	-	-	-	-
CWIP (tang. & intang.)	1,111	1,017	767	217	(333)
Investments (strategic)	-	3,075	3,075	3,075	3,075
Investments (financial)	71	307	307	307	307
Current assets (ex cash)	3,810	3,622	4,365	5,156	5,540
Cash	129	141	178	391	2,618
Current liabilities	798	1,142	1,309	1,548	1,719
Working capital	3,012	2,479	3,056	3,608	3,821
Capital deployed	7,032	10,586	12,420	14,790	18,719
Contingent liabilities	109	-	-	-	-

Fig 4 – Ratio analysis

Year-end: Mar	FY19	FY20	FY21e	FY22e	FY23e
P/E (x)	21.3	12.6	22.1	18.3	15.5
EV / EBITDA (x)	29.5	21.2	17.8	14.7	11.9
EV / Sales (x)	12.3	9.8	8.4	6.9	5.6
P/B (x)	13.6	9.5	7.1	5.5	4.3
RoE (%)	27.7	44.2	36.8	34.0	31.4
RoCE (%) - after tax	24.9	33.7	29.3	29.3	28.4
DPS (Rs / sh)	1.6	5.0	2.8	3.4	4.1
Dividend yield (%)	0.5	1.6	0.9	1.1	1.3
Dividend payout (%) - incl. DDT	24.1	24.1	24.1	24.1	24.1
Net debt / equity (x)	0.1	0.2	0.0	(0.0)	(0.2)
Receivables (days)	82	51	58	58	48
Inventory (days)	88	77	69	68	67
Payables (days)	30	31	27	28	28
CFO : PAT %	63.7	123.8	91.8	96.4	105.7

Source: Company, Anand Rathi Research

Fig 6 – Revenue break-up (Q2 FY21)



Source: Bloomberg

Result highlights

Fig 7 – Quarterly financials

(Rs m)	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	% yoy	% qoq
Sales	2,509	1,974	2,729	1,787	1,848	2,382	2,374	-13.0	-0.4
Gross profit	1,755	1,560	1,819	1,349	1,318	1,675	1,638	-10.0	-2.2
Gross margins (%)	70.0	79.1	66.6	75.5	71.3	70	69	235bps	-132bps
EBITDA	1220	1025	1255	796	773	1121	985	-21.5	-12.1
EBITDA margins (%)	48.6	51.9	46.0	44.6	41.8	47.0	41.5	-450bps	-556bps
Finance expenses	17	38	44	76	72	32	33	-26.2	1.8
Depreciation	60	55	56	56	70	71	75	33.4	6.2
Other income	4	24	54	49	53	57	4	-93.4	-93.8
PBT	1,147	1,130	1,244	777	894	1,179	968	-22.2	-17.8
Tax	399	210	315	198	152	263	228	-27.7	-13.6
Effective tax rate (%)	34.8	18.6	25.3	25.5	17.0	22.4	23.5	-7.1	5.1
Adjusted PAT	748	919	930	579	742	915	741	-20.3	-19.1

Source: Company, Anand Rathi Research

Fig 8 – Revenue break-up

(Rs m)	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	% yoy	% qoq
CDMO pharma	1,138	918	2,068	792	910	1,249	1,442	-30.3	15.4
% of sales	45.9	46.1	75.4	42.8	49.3	52.4	60.7		
CDMO specialty chemicals	1,180	1,005	543	695	800	935	682	25.6	-27.0
% of sales	47.6	50.5	19.8	37.5	43.3	39.3	28.7		
Formulations and other services	159	66.9	132.1	365	138	198	250	89.3	26.1
% of sales	6.4	3.4	4.8	19.7	7.4	8.3	10.5		
Total	2,477	1,990	2,743	1,852	1,848	2,382	2,374	-13.5	-0.3

Source: Company, Anand Rathi Research

Concall highlights, Key takeaways

Guidance

- Suven has maintained its 15-20% PAT growth for FY21 in spite of a weak H1 FY21
- Profit share from the JV may be Rs400m-450m.
- H2 EBITDA margins are expected to be higher than those in H1.
- The timeline for commercialisation of new projects has not changed due to the Covid-19 outbreak.
- Plans to launch one specialty chemical product in H2 FY21 and one each in FY22 and FY23.

Capex plans

- The company has envisaged capex of Rs6bn, largely on automation, technology upgrading and capacity expansion.
- 20-25% of the planned capex will be spent on increasing capacity (it will add a block at Pashamylaram); the rest on refurbishing the existing plant as it plans to scale up a few projects in the near future.
- Modernisation of its facilities is required as it anticipates a pick up in a few projects, critical for future growth.
- The capex amount will be expended over 24-36 months. For each project exact amounts have yet to be allocated. More clarity will emerge by the next quarter.
- In H2 FY21 it plans to incur Rs750m capex for the Vishakhapatnam plant, which is likely to be commercialised in FY22.

Financial Performance

- Q2 profitability was lower due to the product mix and an increase in manufacturing expenses to adhere to environmental norms.
- Employee cost was higher due to a fall in productivity because the Covid-19 pandemic required additional man-hours.
- Formulation sales were Rs101.8m, of which its profit share was Rs20m. Part of the profit share is expected in subsequent quarters.

Stake sale

- The promoters have no plans to sell their stake.

Formulations

- The company filed 11 ANDAs with the US FDA, of which five have been approved and three have been commercialized. Of those commercialised, one is with Taro, two are with separate customers. It plans to launch the other two products in H2 FY21.
- It plans to add 3-4 ANDAs in H2 FY21 and 7-8 products in FY22.
- H1 FY21 formulations sales were Rs180m.
- It plans to launch two ANDAs in H2 FY21.

CDMO pharma

- Added one customer in the last six months.

- New clinical projects have been added now
- In future, Suven might align with its CDMO customers once their products turn generic. Suven may supply APIs and formulations to customers once existing products go generic.
- One molecule is likely to move from phase-2 to phase-3 in H2 FY21. The company anticipates volumes for this product to rise significantly ahead.

Fig 9 – Sales break-up assumptions

(Rs m)	FY21e	FY22e	FY23e
CDMO pharma	5,166	6,125	6,891
% Y/Y	10.4	18.6	12.5
% of sales	53.8	53.6	50.5
CDMO specialty chemicals	3,495	4,020	4,904
% Y/Y	15.0	15.0	22.0
% of sales	36.4	35.2	35.9
Formulations and other services	945	1,276	1,850
% Y/Y	35.0	35.0	45.0
% of sales	9.8	11.2	13.6
Total	9,607	11,421	13,645

Source: Company, Anand Rath Research

Valuations

We lower our FY21e, FY22e and FY23e earnings 3.8%, 3.6% and 3.6% respectively to factor in the lower share of profits from the JV and the rise in depreciation costs due to the new capex.

Fig 10 – Change in estimates

Rs m	Old estimates			New estimates			Change (%)		
	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e
Revenue	9,520	11,311	13,474	9,621	11,440	13,665	1.1	1.1	1.4
EBITDA	4,379	5,203	6,225	4,522	5,399	6,491	3.3	3.8	4.3
PAT	3,760	4,535	5,366	3,618	4,372	5,175	-3.8	-3.6	-3.6

Source: Anand Rathi Research

Suven is likely to see a strong increase in commercial molecules in the CDMO segments and a ramp-up in its formulations business. Over FY21-23 two specialty chemicals products are likely to be commercialised, which would drive the segment's strong double-digit growth. Apart from the four molecules in the pharma segment, one more product is expected to be commercialised in FY22. Besides, in formulations the company will have launched 8-9 ANDAs by end-FY22, each contributing \$2m-4m to profits.

Traction in its CDMO division and steady formulation launches would drive 17.9%/17.7% growth in sales/earnings over FY20-23. At the CMP of Rs314, the stock quotes at 22.1x, 18.3x and 15.5x respective FY21e/FY22e/FY23e earnings. We retain our Buy recommendation with a lower target of Rs375 (earlier Rs380).

Risks

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

Fig 11 – Valuation Summary

Company	RATING	CMP	TP	M Cap	EPS (Rs)			PE (x)			EV/EBITDA (x)			RoE (%)		
		(Rs)	(Rs)	(Rs bn)	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e	FY21e	FY22e	FY23e
Aarti Drugs	Buy	644	813	60.0	28.9	34.5	44.7	22.3	18.6	14.4	14.3	12.0	9.2	35.0	31.6	31.3
Ajanta	Hold	1,604	1,614	140.7	57.8	73.2	87.8	27.8	21.9	18.3	17.3	14.0	11.5	18.1	19.8	20.4
Alembic	Hold	1,011	1,140	198.8	59.3	50.4	63.4	17.1	20.1	16.0	12.5	13.1	10.4	28.9	19.0	20.6
Alkem	Hold	2,652	3,145	317.0	106.0	123.9	136.8	25.0	21.4	19.4	18.8	15.9	14.1	19.2	19.6	18.9
Zydus Cadila	Hold	426	391	436.2	15.1	17.5	19.6	28.3	24.4	21.8	17.1	15.1	13.4	14.3	15.3	15.5
Eris	Hold	492	565	66.8	24.2	26.0	27.9	20.4	18.9	17.6	16.1	14.3	12.6	23.0	20.9	19.2
Granules India	Buy	392	338	97.0	20.6	25.3	30.4	19.0	15.5	12.9	12.5	10.0	8.1	24.7	24.5	23.8
Indoco Remedies	Sell	253	190	23.3	7.5	10.3	12.5	33.6	24.6	20.3	13.7	11.0	9.5	9.7	12.0	12.9
Ipca Labs.	Buy	2,075	2,300	262.2	87.6	90.8	103.5	23.7	22.8	20.1	16.9	15.8	13.5	26.9	22.4	21.0
JB Chemicals	Sell	1,022	760	79.0	43.4	45.9	50.7	23.5	22.2	20.2	15.8	14.5	12.7	21.6	19.8	19.1
Natco Pharma	Hold	929	851	169.1	28.1	31.0	75.7	33.1	30.0	12.3	26.2	22.8	9.3	12.8	12.7	26.3
Neuland	Hold	1,216	880	15.7	36.7	44.5	53.0	33.2	27.3	22.9	14.7	12.8	11.3	6.5	7.4	8.2
Pfizer	Hold	5,013	4,713	229.3	112.4	123.1	131.6	44.6	40.7	38.1	32.8	29.9	27.3	14.4	14.3	13.8
Suven Pharma	Buy	314	375	80.0	14.2	17.2	20.3	22.1	18.3	15.5	17.8	14.7	11.9	36.8	34.0	31.4
Torrent Pharma	Buy	2,654	3,080	449.2	68.7	85.6	104.2	38.6	31.0	25.5	19.8	17.2	14.9	22.5	24.5	25.8

Source: Company, Anand Rathi Research

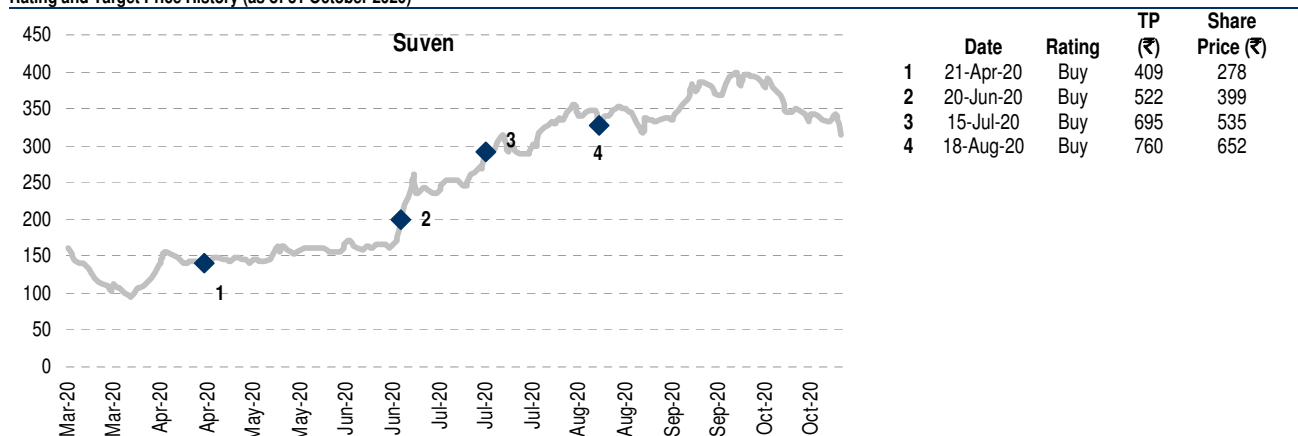
Appendix

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