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Sanofi India

Healthy growth prospects

Pharmaceuticals	Sharekhan code: SANOFI	Company 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	Change
Reco: **Buy**	↔
CMP: **Rs. 8,203**	
Price Target: **Rs. 9,600**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

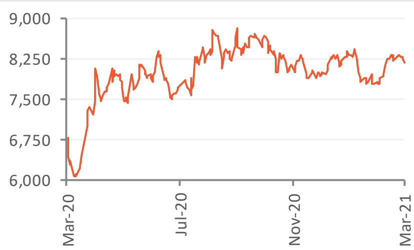
Company details

Market cap:	Rs. 18,890 cr
52-week high/low:	Rs. 8,999 / 5,900
NSE volume: (No of shares)	0.3 lakh
BSE code:	500674
NSE code:	SANOFI
Free float: (No of shares)	91.2 cr

Shareholding (%)

Promoters	60.4
FII	13.6
DII	16.2
Others	9.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.2	2.9	-5.8	20.9
Relative to Sensex	8.9	-3.4	-33.6	-42.0

Sharekhan Research, Bloomberg

Summary

- Sanofi India Limited (Sanofi) had hosted an investor webinar to discuss the business updates and management's commentary was positive pointing at healthy growth outlook.
- Sanofi expects anti-diabetic segment to be a key growth driver for the company. Also the Top10 brands are expected to stage a strong growth and outperform the industry growth.
- Favourable mix and cost efficiencies are expected to result in a 120 bps OPM expansion over CY2020-CY2022E.
- Considering high growth visibility from chronics, strong balance sheet with no debt, minimal capex, and healthy cash position, premium valuations are expected to sustain. We retain Buy with a revised PT of Rs. 9,600.

Sanofi India Limited (Sanofi) had hosted an investor webinar to discuss the business updates and management's commentary was positive, pointing towards a healthy growth outlook for the company. The Indian Pharmaceutical Market (IPM) has recovered posting a growth of ~5% y-o-y for October 2020 - February 2021 as compared to a 2.5% decline in 1HFY2021. Pick-up in IPM is largely driven by growth in chronic therapies. Management expects this trend to sustain going ahead, which bodes well for Sanofi. Further, the company has laid its focus on the anti-diabetic segment for growth, as it has a strong presence in the segment because of a leading position commanded by its brands Lantus and Amaryl. Along with the anti-diabetic segment, Sanofi is present in the cardiology segment, which is one of the fastest growing segments in the IPM. Together, anti-diabetic and cardiac segments constitute around half of the topline. Sanofi's top 10 brands account for around 75% of sales and management expects these to outperform the market's growth, thus pointing at a healthy growth outlook. Moreover, efforts to increase the geographical reach to tier II towns and rural areas would add to revenue growth. Moreover, in CY2020, the company has divested its Ankaleshwar plant, which catered to exports markets. Post the divesture, revenue mix has shifted in favour of the domestic business, which commands higher margins, leading to a favourable mix. Moreover, adaption of the digital platform for reaching out to physicians and enhancing the engagements could bring in some cost efficiencies. Thus, favourable mix and cost efficiencies are expected to result in a 120 bps OPM expansion over CY2020-CY2022E. Consequently, Sanofi's PAT is expected to report double-digit 12% CAGR over CY2020-CY2022E.

Our Call

Valuation: Retain Buy with a revised PT of Rs. 9,600: Sanofi has laid its focus on the anti-diabetic segment for growth going ahead, as it has a strong presence in the segment (through its leading brands – Lantus and Amaryl) and the same is expected to strengthen further. Efforts to enhance geographical penetration and increase physician engagements would be key growth drivers for the segment. Moreover, management expects its top 10 brands to continue outperforming market growth. Moreover, a chronic-heavy portfolio and strong performance of the top brands coupled with a dominant share in their respective categories (due to strong brand positioning) provide comfort on growth ahead. On account of an expected favourable mix (due to divesture of the Ankaleshwar plant) and cost efficiencies, operating profit margin (OPM) is expected to expand by 120 bps y-o-y over CY2020-CY2022E, leading to double-digit 12% earnings CAGR over the same period. At the CMP, the stock is trading at 31.7x/29x its CY2021E/CY2022E earnings. Considering high growth visibility from chronics, strong balance sheet with no debt, minimal capex, and healthy cash position, premium valuations are expected to sustain. We retain our Buy recommendation on the stock with a revised PT of Rs. 9,600.

Key risk

Inclusion of the company's products in the National List of Essential Medicines could have an adverse impact on earnings performance.

Valuation Rs cr

Particulars	CY2018	CY2019	CY2020	CY2021E	CY2022E
Total Sales	2770.8	3070.6	2901.9	3191.9	3417.2
EBIDTA	713.2	759.4	802.9	900.0	980.4
OPM (%)	22.5	21.7	24.6	25.1	25.8
Reported PAT	380.6	473.5	519.3	594.4	649.8
EPS (Rs.)	165.5	205.9	225.8	258.5	282.5
PER (x)	49.6	39.8	36.3	31.7	29.0
EV/EBIDTA (x)	24.6	22.7	21.4	19.0	17.1
P/BV (x)	8.5	7.7	8.9	7.9	7.0
ROCE (%)	25.9	26.0	32.2	33.0	32.1
RONW (%)	17.2	17.0	22.5	24.8	24.0

Source: Company; Sharekhan estimates

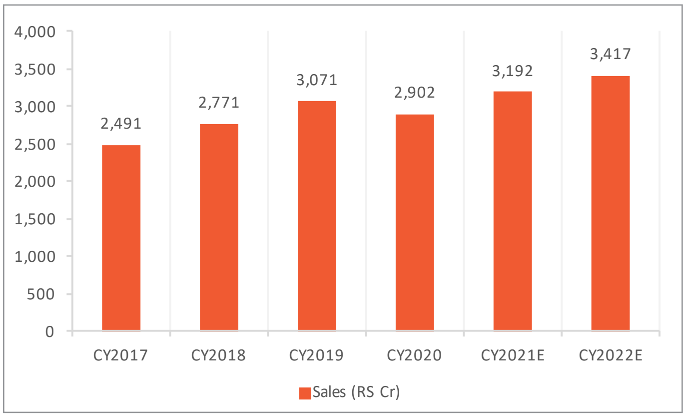
IPM growth to be largely driven by chronics: Sanofi is an India focused MNC company with a large presence in the chronics segment. The company derives a chunk of its revenue from India markets, hence fortunes are linked to that of the IPM. After a decline of 2.5% y-o-y for 1HFY2021, IPM growth has shown signs of revival, reporting 5% y-o-y growth for October 2020 to February 2021. A larger chunk of growth can be attributed to price increases, followed by share of new product introductions, while volumes were on a declining trend. However, overall IPM growth of 5% for October 2020 to February 2021 is an improvement as compared to a decline in 1HFY2021. Pickup in IPM is largely driven by sustained traction in chronic and sub-chronic therapies, while acute therapies are showing signs of pickup. Going ahead, industry reports point that strong pricing growth and share of new products are expected to sustain, which is likely to be complimented by pick-up in volume growth. Collectively, IPM is expected to report double-digit growth in FY2022, and the management expects the growth in IPM to be largely driven by the sustained growth momentum in the chronic segment and this bodes well for chronic heavy companies such as Sanofi.

Sturdy performance of top brands to continue; focus on anti-diabetic segment and geographical expansion to aid topline growth: Sanofi is a chronic-focused company, with the segment constituting a lion's share of the company's revenue. Within chronics, diabetology and cardiology account for around half of Sanofi's domestic sales. The company has a wide portfolio of anti-diabetic medicines, with larger portion of insulins followed by oral solids. In India, Sanofi is among the leading players in the anti-diabetic category. Sanofi's brands such as Lantus and Amaryl command a leading position in the anti-diabetic segment. Lantus has reported sturdy growth of 20% y-o-y as of December 2020 (MAT basis) versus market growth of 8%, while Amaryl has reported strong growth of 9%. Going ahead, management sees the anti-diabetic segment to be a key growth driver as insulinisation rate in India stands at 15%, which is quiet low as compared to other developed nations. Moreover, the company is looking to expand its presence in tier II and rural areas as these have reported strong growth in excess of 12% as compared to a 2%-4% growth reported in tier I towns and cities. Sanofi would be leveraging the digital platform to connect with physicians in these areas and in turn enhance the reach. Sanofi's top 10 brands contribute around 75% of overall sales and are commanding position in their respective categories/segments. Management expects the top 10 brands to report high single-digit growth and is expected to outperform market growth.

OPM expansion to drive earnings growth: During CY2020, Sanofi has divested its Ankaleshwar plant, which was engaged in to the contract manufacturing, catering to requirements of exports markets. Divesture of the plant could result in revenue loss of ~Rs. 470 crore as per management. This is likely to tilt the revenue mix in favour of the domestic segment, which commands higher margins as compared to the exports business, thus resulting a favourable mix. Further, Sanofi is looking to enhance its geographical presence by leveraging the digital platform partly to engage with physicians and is accordingly investing to build the same. We expect the shift to a hybrid model (partly digital and partly personal meeting) to expand the reach could result in operational efficiencies. Collectively, this coupled with a favourable mix could drive margin expansion and OPM is likely to expand by 120 bps over CY2020-CY2022E. This is expected to lead to a 12% earnings CAGR over the same period.

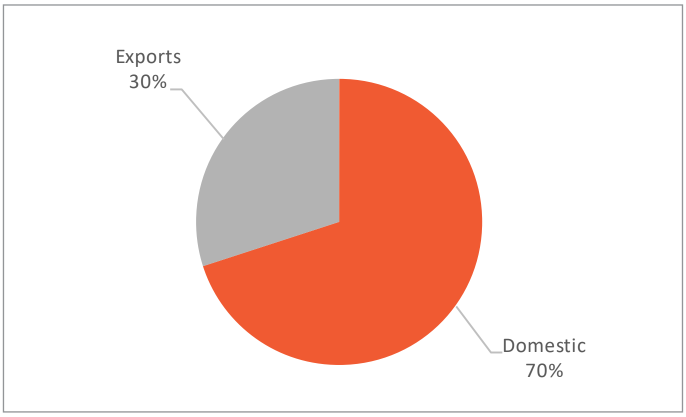
Financials in charts

Sales Trends



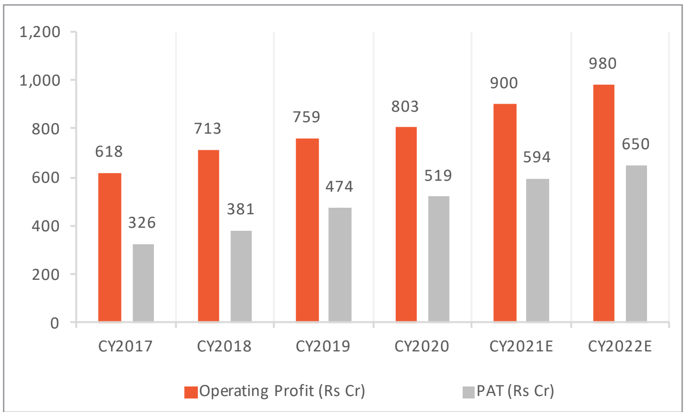
Source: Company, Sharekhan Research

Revenue Mix



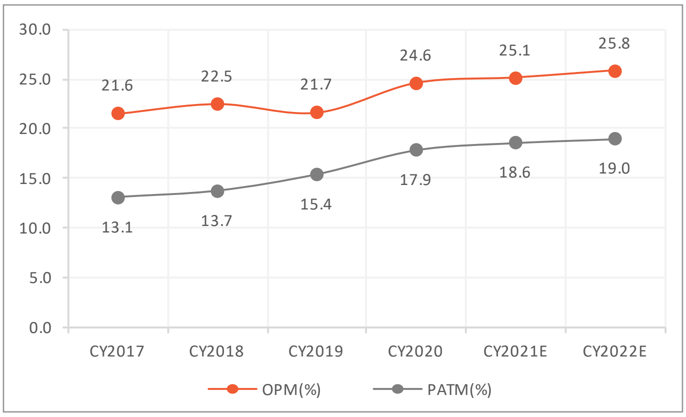
Source: Company, Sharekhan Research

Operating Profit - PAT Trends



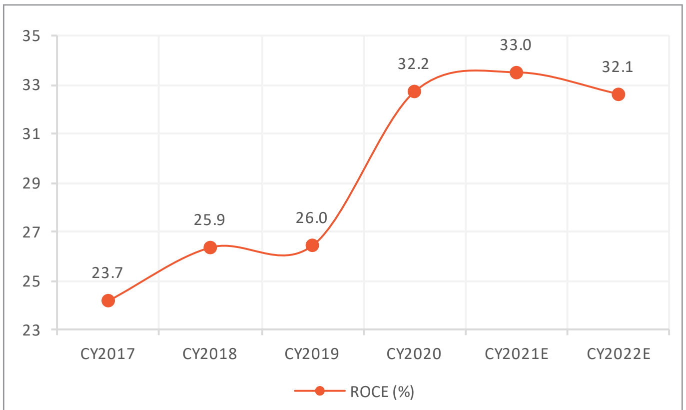
Source: Company, Sharekhan Research

Margin Trends



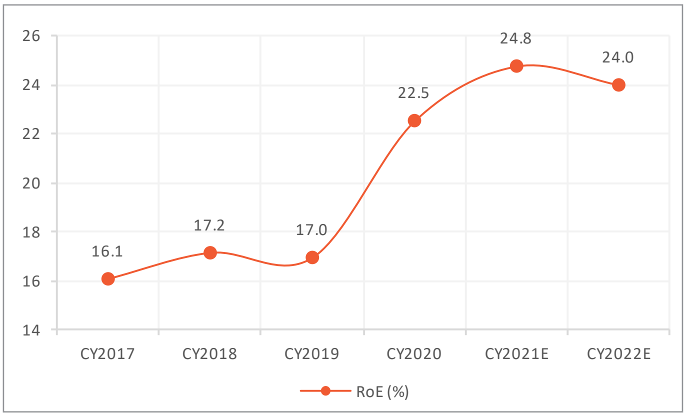
Source: Company, Sharekhan Research

RoCE Trend (%)



Source: Company, Sharekhan Research

RoE (%) Trends



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Growth prospects look better

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.

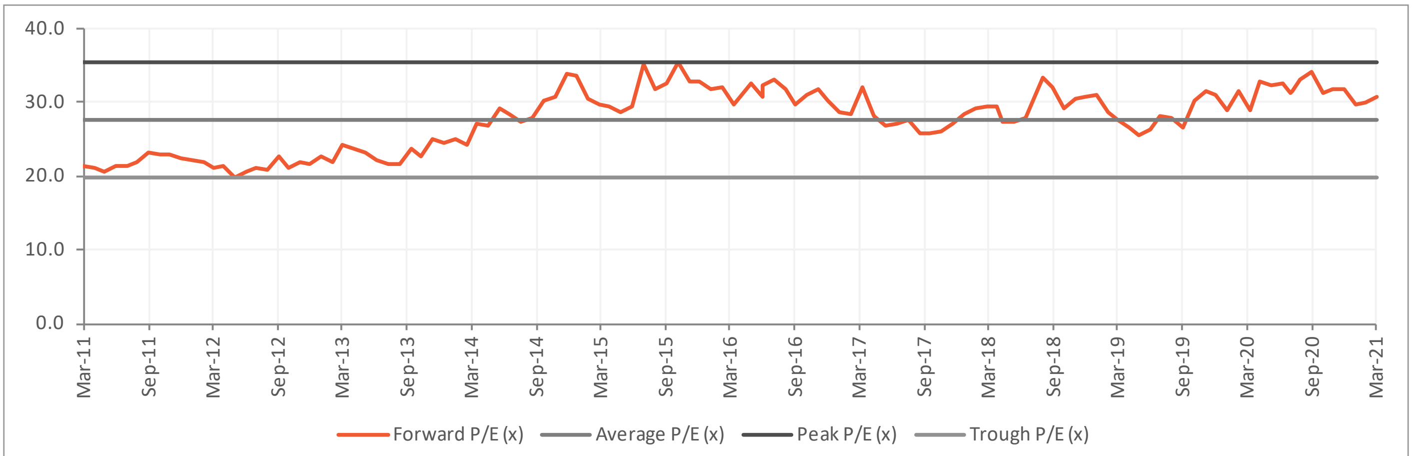
■ Company Outlook – Healthy earnings visibility

Sanofi is one of the leading MNC pharma companies focused on the Indian market. Diabetology is the company's forte and it is among the fastest-growing companies in India in this space. New launches in the space coupled with the strong parentage offer healthy growth for the therapy. In addition to anti-diabetics, cardiology is one of the key segments for the company and is among the fastest growing segments in IPM. A higher share of chronics (more than half of the revenue) points at stable revenue growth going ahead due to sticky demand for products. Moreover, in the overall industry, the chronic segment is a leading growth driver, and this bodes well for Sanofi. Strong growth in the top five brands coupled with OPM expansion (due to a favourable mix) points at sturdy earnings growth.

■ Valuation – Retain Buy with a revised PT of Rs. 9,600

Sanofi has laid its focus on the anti-diabetic segment for growth going ahead, as it has a strong presence in the segment (through its leading brands – Lantus and Amaryl), and the same is expected to strengthen further. Efforts to enhance geographical penetration and increased physician engagements would be the key growth drivers for the segment. Moreover, management expects its top 10 brands to continue outperforming market growth. Moreover, a chronic-heavy portfolio and strong performance of the top brands coupled with a dominant share in their respective categories (due to strong brand positioning) provide comfort on growth ahead. On account of an expected favourable mix (due to divesture of the Ankaleshwar plant) and cost efficiencies, OPM is expected to expand by 120 bps y-o-y over CY2020-CY2022E, leading to a double-digit 12% earnings CAGR over the same period. At the CMP, the stock is trading at 31.7x/29x its CY2021E/CY2022E earnings. Considering high growth visibility from chronics, strong balance sheet with no debt, minimal capex, and healthy cash position, premium valuations are expected to sustain. We retain our Buy recommendation on the stock with a revised PT of Rs. 9.600.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer valuation

Particulars	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)			EV/EBIDTA (x)			RoE (%)		
				CY20	CY21E	CY22E	CY20	CY21E	CY22E	CY20	CY21E	CY22E
Sanofi India	8,203.0	2.3	18,890.0	36.3	31.7	29.0	21.4	19.0	17.1	22.5	24.8	24.0
Abbott India*	14,731.0	2.1	31,302.0	52.8	42.5	38.2	33.4	27.5	24.4	24.4	26.3	25.3

*Source: * Nos for FY20/FY21E/FY22E*

About company

Sanofi was incorporated in 1956 with the name of Hoechst Fedco Pharma Pvt. Ltd. Sanofi is a subsidiary company of MNC pharma giant, Sanofi SA, based in France. In India, the group operates through three main companies – Sanofi India, Shantha Biotechnics through Sanofi Pasteur (the R&D and vaccine business unit), and Sanofi Genzyme, which provides diagnostics and testing services. Of all the three group companies, Sanofi is the largest subsidiary of Sanofi SA and is one of the leading pharma companies in India present in multiple therapies. The company offers a wide array of medicines across therapies such as diabetology and cardiology, vaccines, respiratory, pain, CNS, gastrointestinal, anti-infectives, and dermatology. Sanofi has a manufacturing facility located in Goa. Sanofi primarily derives a chunk of its revenue from domestic markets (~70% as of CY2018), while the balance is generated from exports markets. However, post the recent divesture of the Ankleshwar plant to Zentiva, revenue share from exports is expected to fall drastically as Ankleshwar plant contributed to around 40% to total exports. The company's top five brands, including Lantus, Combiflam, Allegra, Ameryl, and Hexaxim constitute 38%-40% to the company's revenue.

Investment theme

Sanofi is one the leading MNC pharma companies focused on Indian markets. Diabetology is the company's forte; and the company is among the fastest-growing companies in India in this space. Sanofi has a strong parentage from Sanofi SA, which is an MNC pharma major. Higher share of chronics points at stable revenue growth going ahead due to the sticky/inelastic demand for products. Strong growth in the top five brands coupled with OPM expansion points at sturdy earnings growth. High-growth visibility from chronics, low exposure to highly regulated US markets, strong balance sheet with no debt, minimal capex, healthy cash position, and sturdy cash conversion cycle are key drivers that would enable to sustain premium valuations.

Key Risks

- The National List of Essential Medicines is expected to be revised in CY2020; and if in case, any of Sanofi's products are included under this, it would adversely impact growth.
- Any negative impact on the top five brands/high-growth products would impact earnings.

Additional Data

Key management personnel

Mr Aditya Narayan	Chairman
Mr Rajaram Narayan	Managing Director
Mr Vaibhav Karandikar	Whole Time Director & CFO

Source: Company Website

Top 10 shareholders as on 28 July 2020

Sr. No.	Holder Name	Holding (%)
1	Standard Life Aberdeen PLC	3.38
2	Aditya Birla Sunlife Trustee Co	2.97
3	PineBridge Investments	2.79
4	UTI Asset Management Co	2.12
5	Reliance Capital Trustee Co	2.01
6	SBI Funds Management	1.63
7	L&T Mutual Fund trustee Ltd / India	1.13
8	Bajaj Allianz Life Insurance Co	1.1
9	HDFC Life Insurance Co	1.05
10	Vangaurd Group PLC	0.81

Source: Bloomberg

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 detoriating 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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