



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	■	↔	■

ESG Disclosure Score NEW

ESG RISK RATING **36.25**
Updated Jan 08, 2022

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

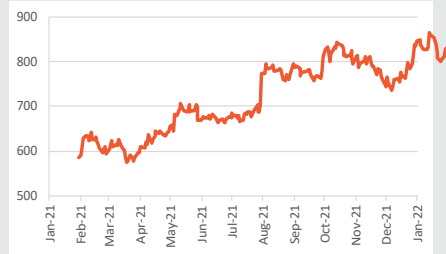
Company details

Market cap:	Rs. 2,00,135 cr
52-week high/low:	Rs. 871 / 554
NSE volume: (No of shares)	40.3 lakh
BSE code:	524715
NSE code:	SUNPHARMA
Free float: (No of shares)	109.2 cr

Shareholding (%)

Promoters	54.5
FII	12.0
DII	21.6
Others	11.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.3	5.0	7.8	42.2
Relative to Sensex	-0.9	7.2	-2.6	16.9

Sharekhan Research, Bloomberg

Sun Pharmaceutical Industries
Strong Q3; Specialty ramp up to drive growth

Pharmaceuticals	Sharekhan code: SUNPHARMA		
Reco/View: Buy	↔	CMP: Rs. 834	Price Target: Rs. 1,000 ↑
↑ Upgrade	↔ Maintain	↓ Downgrade	

Summary

- We retain our Buy recommendation on the Sun Pharmaceutical Industries (Sun Pharma) with a revised PT of Rs 1,000.
- Q3FY22 was a strong quarter and higher other income led to earnings ahead of estimates. The topline and earnings clocked a growth of 11.6% YoY and adjusted PAT grew by 16.2%YoY.
- Strong growth outlook across key geographies of India and US, aided by expanding product portfolio, increasing reach and penetration, growth in base business coupled with traction in global specialty business would be the growth drivers for Sun Pharma.
- Improved growth prospects, healthy financials and strong balance sheet position would be the key positives for Sun pharma.

Sun Pharmaceutical Industries (Sun Pharma) reported strong performance for Q3FY2022 and higher other income led to higher-than-estimated earnings. Performance for the quarter was driven by improved performance across geographies. While global specialty sales grew in strong double digits by 21% y-o-y to \$183 million, India business also grew by 15% y-o-y, led by growth from new launches and, thus, outpaced the industry's growth. Revenue grew by 11.6% y-o-y to Rs. 9,863 crore and adjusted PAT increased by 16.2% y-o-y to Rs. 2,069.4 crore. Robust growth outlook across key geographies of India and US aided by expanding product portfolio, increasing reach and penetration, growth in base business coupled with traction in global specialty business would be key growth drivers for Sun Pharma.

Key positives

- Domestic revenue grew strongly by 15% y-o-y due to new launches and outpaced industry growth.
- Global specialty sales grew by 21% y-o-y to \$183 mn and 9MFY22 sales exceeded FY2021 (full year) sales.
- Emerging market sales grew by 18.8% y-o-y to Rs 1,789.9 crore.

Key negatives

- Operating profit margin (OPM) declined by 158 bps q-o-q due to higher other expenses and raw-material costs.
- Delay in re-inspection and clearance for Halol plant by the USFDA.

Management Commentary

- The global specialty segment's sales for the quarter at \$183 million were up 21% y-o-y. Sun Pharma launched Illumya and Cequa in Canada and Winlevi in the US. Management sees a strong outlook for its specialty portfolio.
- Based on strong uptick across segments in domestic markets, Sun Pharma looks to outpace the domestic industry's growth. New launch momentum has increased substantially with 25 new launches in Q3, which would gain traction in the subsequent quarters.
- Sun Pharma's US generic business is witnessing pricing pressures, but a healthy new product launch pipeline and supply chain efficiencies could offset the impact of price erosion.

Revision in estimates – Sun Pharma reported a strong set of numbers for Q3FY2022 and higher other income resulted in earnings ahead of estimates. Based on this and encouraging outlook across the business, we have fine tuned our estimates for FY2022E/FY2023E/FY2024E.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 1,000: Sun Pharma's key geographies, US and India, are witnessing improved traction. Growth in the US business would be driven by pick up in the specialty business coupled with traction from new product launches and steady growth in US generics. Emerging markets have also gained traction and are expected to sustain the growth momentum. At the CMP, the stock trades at 26.8x/23.5x/20.9x its FY2022E/FY2023E/FY2024E EPS, respectively, which is below the historical long-term average multiple. Improved growth prospects across businesses and healthy balance sheet position would be key positives. We retain our Buy recommendation with a revised price target (PT) of Rs. 1,000.

Key Risks

- Regulatory compliance risk including delay in product approvals;
- Currency risk; and
- Delay in resolution of USFDA observations at Halol plant.

Valuation (Consolidated)

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
Net sales	32837.5	33498.1	38315.6	42327.5	47217.5
Operating profit	6989.8	8491.5	10536.8	11851.7	13457.0
OPM(%)	21.29	25.35	27.50	28.00	28.50
Adj. PAT	4025.6	6801.1	7468.0	8509.8	9577.7
EPS (Rs)	16.8	28.3	31.1	35.5	39.9
PER (x)	49.7	29.4	26.8	23.5	20.9
EV/Ebitda (x)	29.0	23.3	18.2	15.4	12.9
ROCE (%)	9.6	12.7	14.8	15.0	15.4
RONW (%)	8.9	14.6	14.0	13.9	13.6

Source: Company; Sharekhan estimates

Strong quarter: Sun Pharma reported a strong set of results for Q3FY2022. Higher other income led to higher-than-estimated earnings. Performance for the quarter was driven by improvement in performance across geographies. Sales for the quarter at Rs. 9,863 crore grew strongly by 11.6% y-o-y and were in-line with our estimates. India sales were up 15% y-o-y, while US sales grew by 7% y-o-y. The emerging market's revenue also were up in double digits by 18.8% y-o-y. OPM was almost flat on a y-o-y basis at 26.5% but were slightly below estimates due to higher-than-expected raw-material costs and operating expenses. Overall, gross margin for the quarter contracted by 40 bps y-o-y, while savings in employee cost offset the increase in raw-material cost and other expenses. Operating profit at Rs. 2,616.9 crore was up 12.1% y-o-y. Other income at Rs. 432.5 crore was up strongly by 37.3% y-o-y, while interest cost declined by 27.3% y-o-y to Rs. 19 crore. Consequently, PAT stood at Rs. 2,069.4 crore, up 16.2% y-o-y and was marginally ahead of estimates.

Q3FY2022 Conference Call Highlights

- ◆ **Expected traction in the specialty segment to drive US revenue growth:** The US business, which accounts for ~30% of total Q3 sales, is on an improvement path and management sees improving growth traction ahead. Revenue from the US has grown strongly by 7.6% y-o-y and 11% q-o-q. Growth in the US business can be largely attributed to double-digit growth in the specialty business backed by strong growth in the specialty portfolio comprising Cequa, Ilumya, Levulan, and Absorica. The global specialty portfolio reported 21% y-o-y growth in Q3FY2022 and 9MFY2022 revenue has surpassed the FY2021 (full year) sales. Going ahead, the specialty portfolio is expected to witness further market share gains as doctor OPDs fully open up and patient footfalls increase across markets. Currently, patient footfalls are lower and are below pre-COVID levels. However, they are expected to improve, which could lead to higher prescriptions being generated. Moreover, Sun Pharma is in the process of expanding its specialty portfolio to other geographies and has launched Ilumya and Cequa in Canada and Winlevi in the US. In the subsequent quarters, these launches are expected to gain traction. On the generic portfolio, Sun Pharma has launched five new products in Q3 and had launched 10-12 new products in 1HFY2022 and aims to sustain the launch momentum in the subsequent quarters. The company also has developed supply chain efficiencies in US generics and collectively these could help it tide over pricing pressures in the US generics segment. Improvement in the specialty business in the US augurs well and will be a crucial growth factor. In addition to this, Sun Pharma has 88 ANDAs awaiting USFDA approvals. Therefore, pick-up in the US specialty business coupled with a strong product pipeline, which would unfold going ahead and a healthy growth in generics, could be key drivers for the US business.
- ◆ **Domestic formulations grow in double digit:** The India formulations business continued its growth trajectory in uncertain times as well. Revenue from India operations was at Rs. 3,167.6 crore, grew by 15% y-o-y, thus comfortably beating the industry's growth. Double-digit growth can be attributed to strong performance of chronic and acute therapies. The company gained market share in CNS, cardiovascular diseases, and gastro therapy areas. Going ahead, management expects the domestic business to gain traction with all-around growth across therapy areas. Moreover, the company has launched 25 new products in India markets in Q3 (41 new products launched in H1FY2022), while in FY2021, it launched 31 new products, which points at a strong growth momentum and would add to growth going ahead. Further, with the situation normalising, doctor OPDs have almost opened up and footfalls have also improved and are likely to increase. Field force operations are largely close to normal levels for ~70% of field force while the balance 30% is on the path to improvement. Overall, management sees domestic formulations business to grow strongly going ahead backed by new product launches, improving field force productivity, and expected traction in the existing business. Collectively, these factors would drive growth in domestic sales and management looks to outpace the industry's growth.
- ◆ **Other highlights**
 - ◆ Sun Pharma's market share in India stood at 8.1% as of Q2FY2022, as per AIOCD AWACS MAT report. The company has launched 25 new products in the Indian markets (28 products launched as of the quarter ending September 2021) and could sustain the growth momentum.

- ◆ Revenue of emerging markets stood at Rs. 1,789.9 crore, up 18.8% y-o-y. While revenue from Rest of the World (RoW) markets stood at Rs. 1,353.15 crore, up 4% y-o-y.
- ◆ Revenue from the active pharmaceutical ingredients (API) business stood at Rs. 471 crore, growing 4.6% y-o-y. Sun Pharma intends to increase the supplies of APIs for in-house consumption so as to support the formulations segment's growth.
- ◆ Research and development (R&D) spends for Q3FY2022 stood at Rs. 547.1 crore, as compared to Rs. 559.5 crore in Q3FY2021. In the US markets, Sun Pharma has approved ANDAs for 512 products, while 88 ANDAs are pending approval. During Q3, the company received four ANDA approvals. In addition to this, the company's portfolio also includes 53 approved NDAs, while 13 NDAs await USFDA approval.
- ◆ Sun Pharma has repaid \$254 million debt in 9MFY2022 as compared to \$209 million repaid in 1HFY2022.

Results (Consolidated)

Particulars	Rs cr				
	Q3FY2022	Q3FY2021	Y-o-Y %	Q2FY2022	Q-o-Q %
Total sales	9,863.1	8,836.8	11.6	9,625.9	2.5
Operating profit	2,616.9	2,334.5	12.1	2,706.3	-3.3
Other Income	432.5	315.0	37.3	222.9	94.0
EBITDA	3,049.4	2,649.5	15.1	2,929.2	4.1
Interest	19.0	26.1	-27.3	36.0	-47.2
Depreciation	553.7	531.9	4.1	530.4	4.4
PBT	2,476.8	2,091.4	18.4	2,362.9	4.8
Taxes	335.4	244.9	36.9	197.8	69.6
Adjusted PAT	2,069.4	1,780.9	16.2	2,123.4	-2.5
Reported PAT	2,058.8	1,852.5	11.1	2,047.0	0.6
EPS	8.6	7.4	16.2	8.8	-2.5
Margins			BPS		BPS
OPM %	26.5	26.4	11	28.1	-158
PATM %	20.9	21.0	-9	21.3	-39
Tax rate %	13.5	11.7	183	8.4	517

Source: Company; Sharekhan Research

Revenue Mix

Particulars	Rs cr				
	Q3FY2022	Q3FY2021	Y-o-Y %	Q2FY2022	Q-o-Q %
Formulations	9282.4	8322.0	11.5	9058.2	2.5
India	3167.6	2752.8	15.1	3187.8	-0.6
US	2971.8	2762.9	7.6	2677.3	11.0
Emerging Market	1789.9	1507.3	18.8	1800.5	-0.6
ROW	1353.2	1299.1	4.2	1392.6	-2.8
API	471.0	450.5	4.6	435.8	8.1
Others	60.8	36.3	67.4	62.6	-3.0
Total	9814.1	8808.8	11.4	9556.7	2.7
Other Op Inc	48.9	28.0	74.9	69.2	-29.3
Total Sales	9863.0	8836.8	11.6	9625.9	2.5

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Healthy growth momentum to sustain

Indian pharmaceutical companies are better placed to harness opportunities and post 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 and 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 points towards a strong growth potential going ahead for pharmaceutical companies.

■ Company outlook – Better prospects

Sun Pharma, a global pharmaceutical company, is present across a broad spectrum of chronic and acute therapies, which include generics, branded generics, and complex drugs. India and the US are key markets for the company and constitute around 60% of the total topline. Sun Pharma's US business is on the path to improvement, largely backed by marked improvement in the specialty portfolio due to growth in existing geographies as well as tapping new geographies. This coupled with a strong product pipeline, which would unfold going ahead, would be the key growth driver for the US business. Domestic formulations are on a strong footing as the chronic portfolio has reported healthy growth. The acute therapies portfolio has also gathered traction and is expected to sustain the strong growth traction. Management expects the domestic formulations business to continue its strong growth on account of new launches, growth in existing business, field force productivity improvement, and aims to outpace the industry's growth. Therefore, improved outlook across both key geographies, India and US, and increasing penetration in other geographies would drive growth for Sun Pharma.

■ Valuation – Retain Buy with a revised PT of Rs. 1000

Sun Pharma's key geographies, US and India, are witnessing improved traction. Strong growth in chronic therapies along with sustained traction in acute therapies and significant increase in new launch momentum would fuel growth in the domestic formulations business. Growth in the US business would be driven by pick-up in specialty business coupled with traction from new product launches and steady growth in generics. Q3FY2022 was a strong quarter and higher other income led to earnings ahead of estimates. Based on this and an encouraging outlook shared by management, we have fine-tuned our estimates for FY2022E/FY2023E/FY2024E. At the CMP, the stock trades at 26.8x/23.5x/20.9x its FY2022E/FY2023E/FY2024E EPS, respectively, which is below the historical long-term average multiple. Improved growth prospects across business and healthy balance sheet position would be key positives. Therefore, we retain our Buy recommendation on the stock with a revised PT of Rs. 1,000.

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 (%)		
				FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Sun Pharma	834.0	239.9	2,00,135.0	29.4	26.8	23.5	23.3	18.2	15.4	14.6	14.0	13.9
AurobindoPharma	635.0	58.6	37,198.0	15.0	11.1	9.6	6.7	6.0	4.6	12.8	14.3	14.4
Lupin	908.0	45.3	41,257.0	33.9	27.6	20.3	17.7	12.5	9.3	8.8	10.0	12.2

Source: Company, Sharekhan estimates; FY21 Nos are estimates

About company

Sun Pharma is the fourth largest specialty generic pharmaceutical company in the world. Founded in 1983, Sun Pharma has grown to become India's largest pharmaceutical company with global revenue of over \$4 billion. The company manufactures and markets a large basket of pharmaceutical formulations, covering a broad spectrum of chronic and acute therapies, which include generics, branded generics, complex or difficult-to-make technology-intensive products, over-the-counter (OTC) products, anti-retroviral (ARVs), APIs, and intermediates. The company's global presence is supported by over 40 manufacturing facilities. India and the US are predominant markets, accounting for nearly 65% of revenue.

Investment theme

Sun Pharma is a leading pharmaceutical company present across a broad spectrum of chronic and acute therapies, which include generics, branded generics, and complex drugs. India and US are the key markets for the company and constitute around 60% of the total topline. Sun Pharma's US business is witnessing an uptick, largely backed by pick-up in the specialty business and likely pick-up in new product launches. The outlook for the US business has improved on account of a likely revival in the US specialty business coupled with a strong product pipeline, which would unfold going ahead and would be the key growth driver for the US business. Moreover, price erosion is largely stable in the US generic business. Domestic formulations are on a strong footing as the chronic portfolio has reported healthy growth. The acute portion of the portfolio too has gained traction and is expected to sustain the growth momentum, which would be complimented by a strong new launch momentum. Management sees the domestic formulations business to sustain the strong growth momentum and outpace the industry growth.

Key Risks

1) Regulatory compliance risk; 2) Delay in product approvals; 3) Currency risk; 4) Worsening of corporate governance issues; and 5) Negative outcome of ongoing litigations in the US with regards to price collusion.

Additional Data

Key management personnel

Dilip S. Shanghvi	Managing Director
Abhay Gandhi	CEO, North America
C. S. Muralidharan	Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	ICICI Prudential Asset Management	3.4
2	SBI Funds Management Pvt Ltd	2.0
3	Life Insurance Corp of India	6.6
4	HDFC Asset Management Co Ltd	1.52
5	Vanguard Group Inc/The	1.48
6	Nippon Life India Asset Management	1.43
7	Lakshdeep Investments and Finance	1.18
8	BlackRock Inc	1.15
9	Norges Bank	0.75
10	Mirae Asset Global Investments	0.57

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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