Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Sanofi India Ltd

Weak Q2CY22; emphasis on core biz to drive

Pharmaceuticals	Sharekhan code: SANOFI		
Reco/View: Buy ↔	CMP: Rs. 6,604	Price Target: Rs. 8,300 ↓	

↑ Upgrade ↔ Maintain ↓ Downgrade

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 44.39

Updated Feb 08, 2022

Severe Risk

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

Source: Morningstar

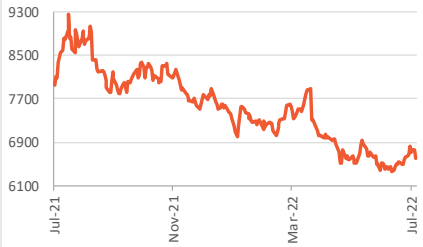
Company details

Market cap:	Rs. 15,209 cr
52-week high/low:	Rs. 9,300 / 6,321
NSE volume: (No of shares)	0.2 lakh
BSE code:	500674
NSE code:	SANOFI
Free float: (No of shares)	91.2 cr

Shareholding (%)

Promoters	60.4
FII	10.3
DII	19.1
Others	10.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	2.6	-6.3	-5.7	-17.3
Relative to Sensex	-2.2	-2.7	-1.2	-21.9

Sharekhan Research, Bloomberg

Summary

- We retain our Buy recommendation on the stock of Sanofi with a revised PT of Rs 8300
- Sanofi has reported a weak result for Q2CY22, though the numbers are not comparable on a y-o-y basis due to divesture of business.
- Emphasis on leveraging the digital platform and divestment of the slow-moving business is expected to drive OPM expansion, leading to a high single-digit PAT CAGR over the next two years.
- High-growth visibility from chronics, strong and debt-free balance sheet, sturdy dividends, and healthy cash position are the key positives. Sanofi has declared a special interim dividend of Rs 193 per share for CY2022.

Sanofi India Limited (Sanofi) has reported a weak performance in Q2CY22 though the results are not comparable on y-o-y basis due to the sale of its nutraceuticals business as well as the sales and distribution business of Soframycin and Sofradex. The results have missed ours as well as street estimates. Revenues declined by 11.4% y-o-y while the PAT declined by 32.4% y-o-y. In addition to the divesture of businesses, a high base in Q2CY21 due to COVID-led demand has also resulted in a y-o-y decline in topline. The company's focus on core areas of diabetology, cardiology, and brand building in consumer products could propel the growth ahead, the divestment of the slow-moving business – Nutraceuticals and Soframycin and Sofradex, recently could enable achieve a linear cost structure, and aid OPM expansion, leading to a high single digit PAT CAGR over the next two years.

Key positives

- Sanofi has declared a special interim dividend of Rs 193 per share for CY2022

Key negatives

- Revenues declined by 11.4% y-o-y to Rs 699.3 cr and missed estimates.
- Gross margins contracted by 230 bps y-o-y, while operating margins contracted by 826 bps y-o-y

Revision in estimates – Sanofi has reported a weak result for Q2CY22, though the numbers are not comparable on a y-o-y basis due to the divesture of business. Given the double-digit decline in topline and PAT for the quarter, we have cut estimates by 5% and 4% for CY22E and CY23E respectively.

Our Call

Valuation – Retain Buy with a revised PT of Rs 8300: Sanofi's plan to emphasize on three areas - accelerating growth in the diabetology space, fortifying presence in established/top brands, and focusing on building brands in consumer products, could be the key growth drivers ahead. Established presence in the chronic therapies, likely growth in insulin products and portfolio expansion in cardiology could also add to the growth. Emphasis on leveraging the digital platform and divestment of the slow-moving business is expected to drive OPM expansion, leading to a high single-digit PAT CAGR over the next two years. High-growth visibility from chronics, strong balance sheet and cashflows, and sturdy dividends are key positives. Sanofi has declared a special interim dividend of Rs 193 per share for CY2022. The stock price has corrected by ~29% from 52-week highs making valuations look reasonable at 26.3X and 23x its CY22E and CY23E EPS. We retain a Buy recommendation on the stock with a revised PT of Rs 8300.

Key Risks

1) Inclusion of the company's products in the National List of Essential Medicines could hurt earnings performance; and 2) Slow growth in top brands.

Valuation Rs cr

Particulars	CY2020	CY2021	CY2022E	CY2023E
Total Sales	2901.9	2956.6	3003.4	3261.8
EBIDTA	802.9	836.9	843.3	958.8
OPM (%)	24.6	25.8	25.6	27.0
Adjusted PAT	519.3	568.2	577.6	659.7
EPS (Rs)	225.8	247.0	251.2	286.8
PER (x)	29.2	26.7	26.3	23.0
EV/EBIDTA (x)	16.9	15.8	16.0	13.8
P/BV (x)	7.2	6.8	7.8	6.8
ROCE (%)	32.2	33.2	38.2	38.4
RONW (%)	22.5	42.5	29.7	29.7

Source: Company; Sharekhan estimates

Weak Q2CY22: Sanofi has reported a weak performance Q2CY22 though the results are not comparable on ay-o-y basis due to the sale of the nutraceuticals business as well as the sale of distribution business of Soframycin and Sofradex. The results have missed ours as well as street estimates. The revenues at Rs 699.3 crore have declined by 11.4% y-o-y attributable to the sale of neutraceuticals business and sale of distribution rights of Soframycin and Sofradex. Also, a high base due to the COVID-led demand for few therapy products has resulted in a double-digit top line de-growth. The operating margins have shrunk sharply by 826 bps y-o-y to 23.1% and missed estimates. A 230 bps y-o-y decline in the gross margins and a 520 bps y-o-y increase in the other expenses/sales resulted in operating margin contraction. Consequently, the EBITDA at Rs 161.2 cr was down by 34.8% y-o-y. Tracking the operating performance, the PAT for the quarter stood at 120.5 cr down by 32.4% and missed estimates.

IPM expected to sustain double-digit growth: Sanofi is an India-focused pharmaceutical company. Hence, growth is reflective of IPM growth. The Indian Pharmaceutical Market (IPM) growth averaged around 10% up to 2019, while it dropped to 4% in January-December 2020 attributable to Covid -19 impact. However, considering a period from January to December 2021, the IPM growth bounced back to 18% as per the IQVIA Prognosis report and the sharp improvement could be attributable to an increase in the demand for acute therapies (anti-infectives, respiratory, gastro, and pain). In addition to this and contribution from COVID-related products drove the growth in the IPM. During this period of January to December 2021, the growth from the chronic areas - like Diabetes and Cardiovascular treatments remained relatively steady. Going ahead, the IPM is expected to grow in double digits over the next one year driven by sustained traction in Acute while chronics and semi-chronics are expected to gain traction. While over the long term the IPM is expected to grow by a double-digit CAGR of around 10-12% over 2020-25. The growth is likely to be driven by improved access to healthcare, an increase in awareness and diagnosis of non-communicable diseases, new product launches, and an expansion of hospital infrastructure. In addition to these aspects, new co-marketing agreements, and expansion of pharmacy chains /online models would also drive the growth of the IPM. Also emerging lifestyle diseases are likely to drive demand for chronic medicines upwards. This bodes well for chronic-heavy companies such as Sanofi.

Chronic therapies to gain momentum bodes well for Sanofi: Sanofi derives a high share of revenues from the chronic focused therapies of diabetology (present in both insulins and orals) and cardiology. In addition to this, it is also present in the areas of thrombosis, epilepsy, allergies, and infections. Its three key products – Lantus, Allegra, and Combiflam have retained leadership in their respective segments and are also amongst the top 100 pharmaceutical brands in India. Sanofi has a wide portfolio of anti-diabetic medicines, with a larger portion of insulins followed by oral solids. In India, Sanofi is among the leading players in the anti-diabetic category. The company looks to fortify its presence further, backed by likely faster growth in key brands such as Lantus. Also in July 2021, the company launched Toujeo in a unique Toustar pen. The concept of the dedicated pen is pioneered by Sanofi. In addition to the insulins, orals – which include brands like Amaryl and Amaryl MV too have been amongst the leading in their respective categories. Both cardiology and anti-diabetes segments have been among the consistently growing therapy areas in IPM and as the demand outlook stays strong. Going ahead, expected traction in key brands – Allegra, Lantus, and Combiflam coupled with new launches is expected to support the growth of Sanofi.

Sanofi lays emphasis on three areas to drive growth ahead: Sanofi has identified three areas, which would propel growth ahead, these include – acceleration in the diabetology (insulins) portfolio, fortifying its presence in the established products through profitable growth, and concentrating efforts on building brands for the consumer portfolio. Further, post divestment of the slow-moving business (Neutraceuticals, Soframycin, and Sofradex), the company is progressing well towards a liner cost structure and has freed up ample bandwidth to focus on core growth areas. Sanofi targets to grow ahead of the industry's growth in covered products, while it is expected to stage 7-8% growth in the established products.

OPMs to expand; while PAT to grow in high single digits: Sanofi's operating margins for Q2CY22 contracted by 826 bps y-o-y to 23.1% largely driven by operating de-leverage and gross margin contraction. However, the margin outlook is healthy driven by a slew of factors. 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. In addition to this, the shift to hybrid model (to expand reach) could yield operational efficiencies. Moreover, the company has divested its slow-growing nutraceuticals business as well as two brands (Soframycin and Sofradex), which were a drag on overall growth and bodes well. Collectively these factors could drive the expansion in operating margins. We expect OPMs to expand by 120 bps to 27% over CY2021-CY2023E. Consequently, the PAT is expected to stage a high single-digit growth of 8% over the same period.

Results (Standalone) **Rs cr**

Particulars	Q2CY22	Q2CY21	Y-o-Y %	Q1CY22	Q-o-Q %
Revenues	699.3	789.1	-11.4	707.0	-1.1
Expenditure	538.1	542.0	-0.7	512.5	5.0
Operating Profits	161.2	247.1	-34.8	194.5	-17.1
Other income	15.7	17.1	-8.2	24.4	-35.7
Interest	0.4	0.5	-20.0	0.4	0.0
Depreciation	10.6	21.1	-49.8	10.9	-2.8
PBT	165.9	242.6	-31.6	207.6	-20.1
Taxes	45.4	64.3	-29.4	-57.8	-178.6
Adjusted PAT	120.5	178.3	-32.4	149.8	-19.6
Reported PAT	120.5	178.3	-32.4	238.4	-49.5
Adj. EPS	52.4	77.5	-32.4	65.1	-19.6
Margins			**BPS**		**BPS**
OPM %	23.1	31.3	-826	27.5	-446
Adj PAT Margins (%)	17.2	22.6	-536	21.2	-396
Tax Rate (%)	27.4	26.5	86	-27.8	5,520

Source: Company; Sharekhan Research

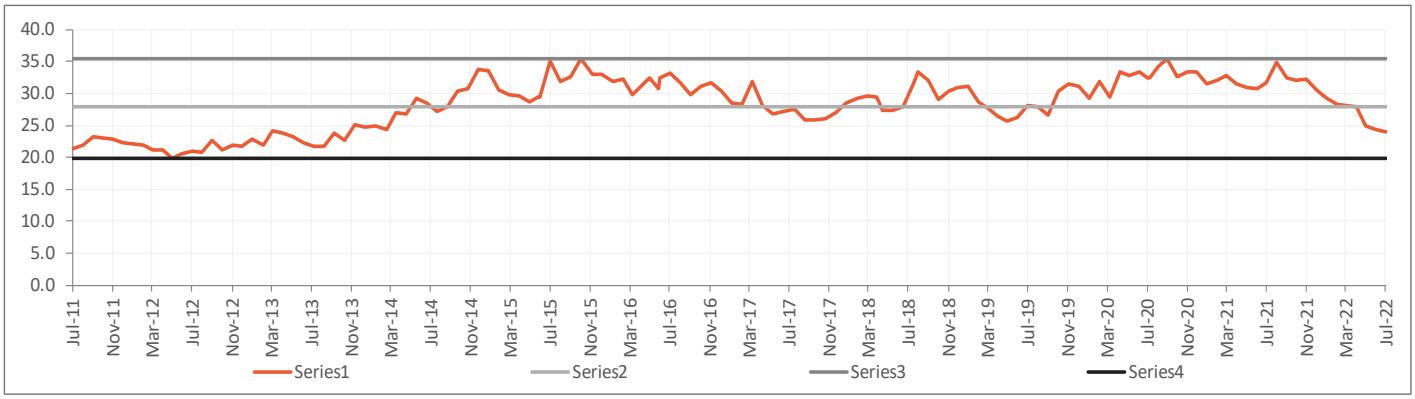
Outlook and Valuation

■ **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, 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 the commissioning of expanded capacities by select players over the medium term. Collectively, this indicates a strong growth potential going ahead for pharmaceutical companies.

■ **Company outlook – Healthy earnings growth:** Sanofi is an MNC pharmaceutical company focused on the Indian market. Diabetology is the company's forte and it is among India's fastest-growing companies in this space. New launches in diabetology and a strong parentage point to healthy growth prospects. In addition to anti-diabetic, cardiology is one of the key segments for the company. Sanofi is also present in the respiratory space, which is also a key segment in the IPM. A higher share of chronic (that fetches more than half of the revenues) points to stable revenue growth going ahead due to sticky demand for products. Moreover, in the overall industry, the chronic segment has staged a steady growth, and going ahead the growth momentum is expected to pick up largely driven by a likely emergency of lifestyle diseases. Strong growth in the top brands and OPM expansion point to sturdy earnings growth. Further, post the divesture of the Ankaleshwar unit, the company as a part of a strategic review has also divested its nutraceuticals business along with its slow-moving brands (Soframycin and Sofradex) and this would help Sanofi set a higher focus on its key growth pillars.

■ **Valuation – Retain Buy with a revised PT of Rs 8300:** Sanofi's plan to emphasize three areas - accelerating growth in the diabetology space, fortifying presence in established/top brands, and focusing on building brands in consumer products, could drive growth. Established presence in the chronic therapies of diabetology with likely strong growth in insulin products and portfolio expansion in cardiology could also add to the growth. Emphasis on leveraging the digital platform and divestment of the slow-moving business is expected to drive OPM expansion, leading to a high single-digit PAT CAGR over the next two years. Sanofi has reported a weak result for Q2CY22, though the numbers are not comparable on a y-o-y basis due to divesture of business. Given the double-digit decline in topline and PAT for the quarter, we have cut estimates by 5% and 4% for CY22E and CY23E respectively. At the CMP, the stock trades at 26.3x/23x, respectively, its CY22E/CY23E estimates. High-growth visibility from chronics, strong and debt-free balance sheet, sturdy dividends, and healthy cash position are the key positives. Sanofi has declared a special interim dividend of Rs 193 per share for CY2022. We retain our Buy recommendation on the stock with a revised PT of Rs 8300,.

One-year forward P/E (x) band



Source: Company, Sharekhan Research

Peer valuation

Particulars	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)			EV/EBITDA (x)			RoE (%)		
				CY21	CY22E	CY23E	CY21	CY22E	CY23E	CY21	CY22E	CY23E
Sanofi India	6,604.0	2.3	15,209.0	26.7	26.3	23.0	15.8	16.0	13.8	42.5	29.7	29.7
Abbott India*	19,426.0	2.1	41,279.0	51.7	45.6	40.0	33.2	29.6	25.9	28.3	29.2	29.3

*Source: Company, Sharekhan estimates; *Numbers for FY22/FY23E/FY24E.*

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 export markets. However, post the recent divesture of the Ankaleshwar plant to Zentiva, revenue share from exports is expected to fall drastically as the Ankaleshwar plant contributes to around 40% to total exports. The company's top five brands, including Lantus, Combiflam, Allegra, Ameryl, and Hexaxim, constitute 38-40% of the company's revenue.

Investment theme

Sanofi is one of the leading pharma MNCs focused on the Indian market. 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. A higher share of chronic points to 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 to 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

- Inclusion of Sanofi's products in the National List of Essential Medicines could adversely impact growth.
- Any negative impact on the top brands/high-growth products would impact earnings.

Additional Data

Key management personnel

Mr. Aditya Narayan	Chairman
Mr. Rodolfo Hrosz*	Managing Director
Mr. Vaibhav Karandikar	Whole-Time Director & CFO

*Source: Company Website; *appointment with effect from 1st June 2022*

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp Of india	5.94
2	Aditya Birla Sunlife Trustee Co	2.93
3	Nippon Life India Asset management	2.00
4	ICICI Prudential Asset management Co	1.93
5	HDFC Life Insurance Co	1.17
6	Bajaj Allianz Life Insurance Co	1.13
7	UTI Asset Management Co	1.12
8	Vangaurd Group Inc	1.07
9	SBI Funds management	0.86
10	Mathews International Capital management	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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