Stock Update

Result Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Torrent Pharmaceuticals Ltd

Healthy Q1; Promising outlook

Pharmaceuticals	Sharekhan code: TORNTPHARM
Reco/View: Buy ↔	CMP: **Rs. 1,529** · Price Target: **Rs. 1,820** ↑

↑ 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 38.1

Updated Feb 08, 2022

High Risk

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

Source: Morningstar

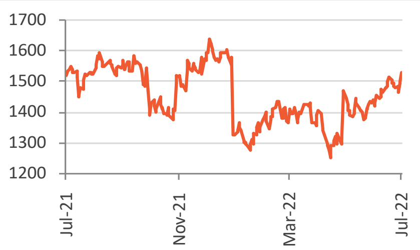
Company details

Market cap:	Rs. 51,739 cr
52-week high/low:	Rs. 1652/1243
NSE volume: (No of shares)	2.2 lakh
BSE code:	500420
NSE code:	TORNTPHARM
Free float: (No of shares)	9.8 cr

Shareholding (%)

Promoters	71.3
FII	11.0
DII	10.1
Others	7.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.7	8.9	14.4	0.7
Relative to Sensex	-0.9	8.0	15.2	-8.7

Sharekhan Research, Bloomberg

Summary

- Torrent Pharmaceuticals Limited (Torrent) reported healthy performance for Q1 and the results are ahead of estimates. Performance reflected the double digit growth in Brazil, India business.
- Torrent sees a healthy outlook for India as well as the Brazil business, backed by expanding reach, market share gains, new product pipeline. It aims to outpace the Industry growth in both these markets.
- The US business is witnessing heightened competitive intensity and price erosion, thus pressurising US sales. Europe sales likely to improve gradually over the next quarter
- Given better growth prospects across Indian and Brazilian businesses, we retain our Buy recommendation on the stock of with a revised PT of Rs 1820.

Torrent Pharmaceuticals Limited (Torrent) reported healthy performance for Q1FY2023 and the results were ahead of estimates. Sales grew by 10% y-o-y while the adjusted PAT was up 7.3% y-o-y. The performance was aided by double-digit growth in the Brazil, and the India business while German sales continued to decline. Going ahead, India and Brazil business could be the company's key growth drivers, while US business is likely to be under stress due to prolonged delays for plant re-inspection by USFDA, leading to a lack of new launches and high competitive pressures. Cost savings due to discontinuation of liquids business and other cost-control measures implemented could result in operating profit margin (OPM) expansion for FY2023.

Key positives

- Domestic business revenue grew by 14% y-o-y, led by outperformance across therapy areas and new launches.
- Brazil's revenue grew by 20% y-o-y, led by strong growth in the generic segment, performance of top brands and new launches.

Key negatives

- Delay in the resolution of OAI/WL at Indrad and Dahej plants.
- Germany sales declined by 18% y-o-y due to loss of tenders and price pressures.

Management Commentary

- Domestic business is on a strong footing and focuses on growing the trade generics business, strong growth in branded generics, expanded field-force, and strong product pipeline could be key growth drivers for India business.
- Torrent envisages Brazil as the key growth driver going ahead backed by a strong product pipeline and plans to double the presence in the covered market.
- The US business is witnessing heightened competitive intensity, leading to double-digit price erosion, thus pressurising US sales. Europe sales likely to improve gradually over the next 2-3 quarters.

Revision in estimates – Torrent reported healthy performance for Q1FY2023 and the results were ahead of estimates. The performance was backed by a double-digit growth in Brazil and the domestic business. This coupled with an encouraging management commentary and an expected healthy margin trajectory, we have revised upwards our estimates by 1% to 4% for FY2023E - FY2024E.

Our Call

Valuation – Bright prospects for India and Brazil; Retain Buy: Torrent sees a healthy outlook for India business, backed by expanding reach, market share gains, and likely traction in the new trade generics division. Expected growth in the existing portfolio, and plans to fortify presence in the covered markets, would drive Brazilian sales growth, while elevated cost pressures, price erosion, and delays in re-inspection for plants by USFDA could slow down US growth momentum. At CMP, the stock trades at 33.2x/27.1x its FY2023E and FY2024E. Given better growth prospects across Indian and Brazilian businesses, we retain our Buy recommendation on the stock with a revised PT of Rs 1820.

Key Risks

Delays in the resolution of USFDA issues at its plants and heightened competitive pressures in the US.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Net sales	8005.0	8508.0	9427.0	10736.0
OPM (%)	31.0	28.6	30.5	32.0
Adjusted net profit	1252.0	1262.0	1566.9	1916.9
EPS (Rs)	36.8	37.1	46.1	56.4
PER (x)	41.5	41.2	33.2	27.1
EV/Ebidta (x)	22.8	22.9	19.4	15.8
P/BV (x)	8.8	8.6	7.4	6.2
ROCE (%)	16.9	18.4	23.2	27.0
RONW (%)	23.1	21.1	24.0	25.0

Source: Company; Sharekhan estimates

Healthy Q1, results ahead of estimates: Torrent reported healthy performance for Q1FY2023 and the results were ahead of estimates. Sales grew by 10% y-o-y to Rs. 2,347 crores, backed by 20% , 14% and 13% y-o-y growth in the Brazil, India and the US business respectively. While Europe (Germany) sales declined by 18% y-o-y. Sales were marginally ahead of estimates. Operating profit margin (OPM) at 30.3% (better than estimates) contracted by 139 bps y-o-y, but expanded by 401 bps Q-o-q. The contraction in the gross margins can be attributable to a 100 bps increase in other Expenses / sales while the raw material costs surged 60 bps. Operating profit stood at Rs. 712 crore, up 5.2% y-o-y and 26.9% Q-o-q. The y-o-y increase can be attributable to the benefits of operating leverage playing out. Tracking the operating performance, the PAT for the quarter stood at Rs 354 crore up 7.3% y-o-y and was above our as well as streets estimates.

Q1FY2023 Concall Highlights

- **India business outpaces industry growth:** Torrent's India business largely comprises the domestic formulations business, which has staged healthy growth of 14% y-o-y to Rs. 1245 crore in Q1FY2023, thus outperforming the Indian pharmaceutical market's (IPM) growth. As per AIOCD, the company growth is 17% which is way higher than the industry growth. Strong performance can be attributed to the strong performance of top brands and new launches as the company outpaced IPM growth and continued its market outperformance in focused therapies. Going ahead, a slew of growth triggers is expected to drive the performance of India business. The company aims to launch 7-8 new products in the Indian markets per quarter which point at a substantial new launch momentum. Also, it had a strong launch momentum in the previous quarters which is now likely to ramp up and add to the growth. The company has added around 300 field force in Q4FY2022 and has added another 300 in Q1FY23 taking the total count to 600 reps. Based on this, Torrent looks to increase coverage across therapies of cardiovascular, CNS, and gastro. Torrent had launched its trade generic division in India in the previous quarter and has received good response since then. Currently, the trade generics business accounts for 2.5% of the India business and given the fast growth pace, the contribution is expected to increase. In addition, strong traction is expected to sustain in the branded generics business, which would also add to revenue growth. Overall, focus on growing the trade generics business, strong growth in branded generics increased field force numbers, and a strong product pipeline could be key growth drivers for the domestic business. Therefore, based on the above drivers, Torrent expects to outpace IPM growth in FY2023, which bodes well.

- **Robust outlook for the Brazil markets:** Revenue from Brazil grew impressively by 20% y-o-y to Rs. 184 crore, while constant currency sales growth was 8%. Growth can be attributed to growth in the overall Brazil market, the strong performance of the top brands, new launches and strong growth in the generic brands. Currently in the Brazil markets, Torrent is present in the speciality segment which includes the CNS, Cardiovascular and diabetes and around 83% of sales are generated through prescriptions. Currently in the covered markets in Brazil Torrent has a presence in 22% of the market and going ahead plans to double the coverage in the next three years. Also in the recent past, the company has launched 5 new products and has around 8 approvals to be launched. It has 11 products in Brazil awaiting clearance and expects the filling momentum per year to be in double digits. Overall given the string presence in the Brazil markets, a strong product pipeline and plans to double the presence in the covered market, the growth outlook stays robust and Torrent expects to outpace the industry's growth in Brazil for FY2023. The industry's growth in Brazil is pegged at 10-12%.

- **Heightened competitive pressures to impact US business growth:** Torrent's US business has been under severe stress as two of its key plants catering to US markets – Dahej and Indrad – have been under USFDA's scrutiny. This affected the base business as well as new product launches, with the new launch momentum hitting severely. US sales for the quarter stood at Rs. 299 crore, which is a growth of 13% y-o-y and includes RS 38 cr as one-time income received from an innovator. Going ahead, management sees US business to be under stress in the near term to medium term as competitive intensity is on the higher side and a sustained price erosion, which could also impact margins. Moreover, as the company's plants are under USFDA scrutiny, the new product launch momentum has been slow and would improve only with regulatory approvals flowing in. Torrent has a strong product pipeline comprising 60 ANDAs pending approval 3 tentative approvals were received in Q1FY23 and during the quarter one ANDA was filled. Overall, due to higher-than-expected competitive intensity, and lack of new product approvals flowing in due to delayed regulatory clearance in Dahej and Indrad, the performance in US markets, could be under stress in the near to medium term.

- **European (Germany)** sales declined by 18% y-o-y to Rs. 214 crores. Performance was impacted by muted market growth and increased competitive pressures in the tender segment, in which the company lost a few tenders and expected new tenders to come in around 2HFY2023. Till then, the performance of European markets is expected to be soft and however post that a material improvement is expected.
- **Margins:** Torrent's OPM declined 139 bps y-o-y, to 30.3% which can be attributed to a 60 bps y-o-y contraction in gross margins due to cost pressures and a 100 bps increase in other exp / sales. However, going ahead, the company is working on certain measures, including production rationalisation at its facilities (to improve utilisation levels), cost-optimisation measures, price hike in branded generic markets, and likely operating leverage kicking in. Further, Torrent expects higher freight costs to normalise over the next two quarters. Secondly, the company has decided to shut down the liquids plant at Levittown, US, as lower utilisation levels are added to costs. Consequently, due to this, management expects savings of Rs. 135 crore per year on the operating cost, which translates into 150-bps on the margins front. Therefore, based on this and benefits from cost-rationalisation measures, management expects OPM for FY2023 to expand by 100-150 bps.

Results (Consolidated) Rs cr

Particulars	Q1FY23	Q1FY22	Y-o-Y %	Q4FY22	Q-o-Q %
Total Sales	2,347.0	2,134.0	10.0	2,131.0	10.1
Operating profit	712.0	677.0	5.2	561.0	26.9
Other income	30.0	40.0	-25.0	56.0	-46.4
EBITDA	742.0	717.0	3.5	617.0	20.3
Interest	55.0	68.0	-19.1	57.0	-3.5
Depreciation	155.0	165.0	-6.1	162.0	-4.3
PBT	532.0	484.0	9.9	398.0	33.7
Taxes	178.0	154.0	15.6	31.0	474.2
Adjusted PAT	354.0	330.0	7.3	367.0	-3.5
Margins			**BPS**		**BPS**
OPM %	30.3	31.7	-139	26.3	401
Adj PATM %	15.1	15.5	-38	17.2	-214
Tax %	33.5	31.8	164	7.8	2,567

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Growth momentum to improve

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 the easing of pricing pressures (especially in the US generics market), rise in product approvals, plant resolutions by the USFDA, 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.

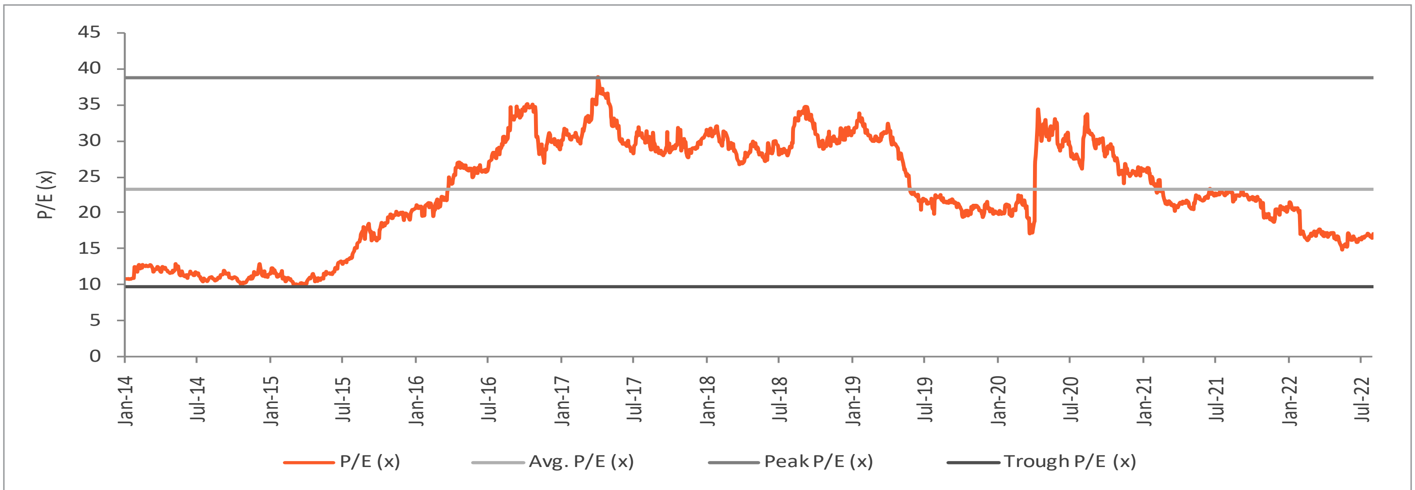
■ Company outlook - Indian and Brazilian businesses to stage strong growth

Torrent is a leading pharmaceutical company present in emerging as well as developed markets. The company has a higher exposure to chronic therapies. Moreover, the company derives a substantial portion of its sales from India, followed by the US, Germany, and Brazil, which collectively form the core markets. The company has been outperforming in the Indian as well as Brazilian markets and management expects to sustain traction going ahead as well and sees these geographies as key growth drivers. Moreover, the German business is expected to gain traction and stage strong growth ahead, backed by growth in the base business and new product launches. The company's US business has been under pressure as two of its plants, which cater to US markets – Dahej and Indrad – are under the USFDA's scanner with OAI/WL classification. However, the Levittown plant has commenced operations and the company expects to launch a new product in the US market from the plant, which could help it mitigate pricing pressures. A timely and successful resolution of these USFDA observations at its two plants is critical and could result in earnings upgrades upon resolution.

■ Valuation - Retain Buy with Revised PT of Rs 1820

Torrent expects a strong outlook for the India business, backed by expanding reach, field force addition, strong new launch pipeline, and market share gains, while it had also set up a trade generics division to focus on acute therapy products with an objective to expand its product portfolio and gain market share. Expected healthy growth in the existing portfolio, likely outperformance in the industry, and new product launches would drive Brazilian sales growth. Management sees India and Brazil as key growth drivers, while it sees European performance to improve gradually towards 2HFY2023. US sales are expected to be under stress, marred by pricing erosion, while Dahej and Indrad plants continue to be under USFDA's scrutiny. A successful resolution for both the plants is awaited and would lead to increased new launch momentum in the US. Torrent reported healthy performance for Q1FY2023 and the results were ahead of estimates. The performance was backed by a double-digit growth in Brazil, India and US business. This coupled with an encouraging management commentary and an expected healthy margin trajectory, we have revised upwards our estimates by 1% to 4% for FY2023E - FY2024E. At the CMP, the stock trades at 33.2x/27.1x its FY2023E and FY2024E. Given better growth prospects across Indian and Brazilian businesses, we retain our Buy recommendation on the stock with a revised PT of Rs 1820.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Companies	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)			EV / EBITDA (x)			RoE (%)		
				FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Torrent Pharma	1529	16.99	51739	41.2	33.2	27.1	22.9	19.4	15.8	21.1	24.0	25.0
Cipla	978.0	80.6	78935	28.8	25.4	20.0	17.1	15.4	12.4	14.6	13.9	15.4

Source: Company, Sharekhan Research

About company

Torrent, the flagship company of Torrent Group, was incorporated in 1972. Torrent has a strong international presence across 40 countries with operations in regulated and emerging markets such as the US, Europe, Brazil, and RoW. The company operates through its wholly owned subsidiaries spread across 12 nations with major setups in Brazil, Germany, and the US. The company is also one of the leading pharmaceutical companies present in India as a dominant player in the therapeutic areas of cardiovascular (CV) and central nervous system (CNS). The company also has a significant presence in gastro-intestinal, diabetology, anti-infectives, and pain management segments.

Investment theme

Torrent continues to focus on a branded business mix from India and Brazil, which balances well for sustainable growth in a challenging global environment for the pharma sector. US business is also stable. Operating leverage from the acquired domestic business is likely to be visible from FY2020. Three manufacturing plants of Torrent are reeling under regulatory issues with a warning letter being issued by the USFDA. Management expects at least 12-15 months for the issues to be resolved; and till such time, approvals from these plants would be withheld. Torrent has submitted its responses to the regulator and is awaiting a revert on this. Timely and successful resolution of USFDA issues is critical from a growth perspective.

Key Risks

- Slowdown in ANDA approvals and USFDA-related regulatory risks could hurt business prospects.
- Delay in product launches in Brazil, Germany, and the US could restrict growth in these key geographies.
- Currency fluctuation poses a risk to export businesses.

Additional Data

Key management personnel

Mr. Sudhir Mehta	Chairman (Emeritus)
Mr. Samir Mehta	Executive Chairman
Mr. Sudhir Menon	CFO

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Mirae Asset Global investment Company	2.14
2	UTI Asset Management Co Ltd	1.37
3	FMR LLC	1.31
4	Blackrock Inc	0.88
5	Vangaurd Group Inc	0.87
6	Pictet Funds SA	0.76
7	T Rowe Price Group Inc	0.72
8	Kotak Mahindra Asset Management Co	0.62
9	Norges Bank	0.5
10	ICICI Prudential Life Insurance Co	0.48

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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