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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	36.3			
Updated Dec 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. 52,033 cr
52-week high/low:	Rs. 1652/1243
NSE volume: (No of shares)	2.6 lakh
BSE code:	500420
NSE code:	TORNTPHARM
Free float: (No of shares)	9.7 cr

Shareholding (%)

Promoters	71.3
FII	11.5
DII	9.5
Others	7.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	4.1	5.4	15.2	2.2
Relative to Sensex	0.3	-0.9	11.8	4.9

Sharekhan Research, Bloomberg

Torrent Pharmaceuticals Ltd

Mixed quarter, USFDA OAI status for facilities act an overhang

Pharmaceuticals	Sharekhan code: TORNTPHARM		
Reco/View: Buy	↔	CMP: Rs. 1,537	Price Target: Rs. 1,788
↑ Upgrade	↔ Maintain	↓ Downgrade	

Summary

- Torrent Pharmaceuticals Limited (Torrent) posted strong revenue growth (after including Curatio's acquisition). As a result, the company outperformed our revenue estimates. However, the result was in line on the operating front; but performance was far below the expectations on PAT basis.
- Revenue growth was driven by strong growth across markets.
- Management has guided that Brazil market will lead growth and Germany should have a steady sequential recovery in the short-medium term. Also, outlook in the US depends on its ability to bring in new products in the market.
- We maintain our Buy rating on Torrent Pharma with a revised PT of Rs. 1,788, as we believe while the subdued outlook on the US with two of its facilities being under OAI by the USFDA can restrict robust product launches, strong growth outlook on India market and Brazil expected to outperform the industry growth should drive its earnings at a better trajectory than estimated before.

Torrent Pharmaceuticals Limited (Torrent) delivered a mixed performance in Q3FY2023. The company's revenue grew by 18.2% y-o-y to Rs. 2,491 crore, while OPM expanded by 354 bps y-o-y to 29.1% in Q3FY2023. PAT for the quarter grew at 13.7% YoY (-9.3% QoQ) to Rs. 283 crore. Strong recovery in sales growth across its major markets helped the company to report strong revenue growth, besides driven by integration of Curatio's product portfolio, while Germany recovered marginally on a y-o-y basis. Management has guided that the Brazil market will continue to lead growth and Germany should have steady sequential recovery in the short-medium term. Management believes the outlook in the US depends on its ability to bring in new products in the market. The company's Indrad and Dahej facilities are under OAI.

Key positives

- Strong recovery across major geographical segments y-o-y in Q3FY2023 vs. in Q2FY2023.
- Torrent's India revenue grew in line with the market in Q3FY2023. The company expects to grow above market growth rates in Brazil in FY2023 and FY2024.
- The company expects pricing growth in the 7-8% range to continue in the upcoming quarters in India, which has been the major driver of its sales growth in India, in case of key products such as Sitagliptin and Pregabalin.

Key negatives

- Delay in the resolution of OAI/WL at Indrad and Dahej plants.

Management Commentary

- Revenue growth was led by strong growth in the branded generics' market (70.0% of revenue) and steady performance in the generics business. Growth in branded generics was driven by new launch momentum, performance of the top brands, and integration of the acquired product portfolio.
- The company's board approved an interim dividend of Rs. 14 per share.
- In India, growth was aided by the new launch performance, especially in the chronic segment, performance of its top brands, and strong growth of the Curatio portfolio. At the end of the quarter, the company has 19 brands in the top 500 of the IPM, with over 13 brands having revenue of more than Rs. 100 crore of sales.
- The company expects India business to continue to fare well, backed by new product launches, top brands' performance, improving field force's productivity, and continued performance of the acquired companies' products, Curatio Healthcare.
- Germany is expected to grow in single-digit rate with tender business wins from earlier period, next year.
- Outlook in the US depends on its ability to bring in new products in the market. The company plans to file 5-6 new products in FY2023. As of December 2022, 48 ANDAs were pending approvals from the USFDA.

Revision in estimates – Torrent reported mixed performance in Q3FY2023. Nevertheless, with a strong outlook on India and Brazil markets, partially offset by weaker outlook on the US, we maintain the sales growth CAGR estimate at 12.3% but increase our earnings CAGR estimate to 19.5% CAGR from 17.1% CAGR estimated earlier during FY2022-FY2025E.

Our Call

View: Maintain Buy with a revised PT of Rs. 1,788: Torrent's Q3 performance was mixed. However, the company expects Brazil market to continue to lead the growth and Germany should have steady sequential recovery in the short-medium term. The company expects India business also to continue to fare well, backed by new product launches, top brands' performance, improving field force's productivity, and continued performance of the acquired companies' products, Curatio Healthcare. However, outlook in the US appears subdued, as it depends on its ability to bring in new products in the market. The company plans to file 5-6 new products in FY2023. At the same time, as of December 2022, 48 ANDAs were pending approvals from the USFDA, while its Indrad and Dahej facilities are under OAI. At the CMP, the stock trades at 31.0x/24.2x its revised FY2024E/FY2025E EPS. Given the improved outlook on the earnings front, we maintain our rating on the stock to Buy with a revised price target (PT) of Rs. 1,788, as we value it at 28.2x its revised FY2025E EPS vs. 30.5x multiple used earlier, as the stock indicates an upside potential of 16% from its CMP.

Key Risks

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

Valuation (Consolidated)

Particulars	Rs cr				
	FY21	FY22	FY23E	FY24E	FY25E
Net sales	8,005.0	8,508.0	9,338.2	10,657.3	12,042.9
OPM (%)	31.0	28.6	29.5	31.5	32.5
Adjusted net profit	1252.0	1262.0	1231.2	1687.2	2155.8
EPS (Rs)	36.8	37.1	36.2	49.6	63.4
PER (x)	41.8	41.4	42.5	31.0	24.2
EV/EBITDA (x)	22.9	23	20.5	16.5	13.7
P/BV (x)	8.8	8.7	7.8	6.7	5.6
ROCE (%)	16.9	18.4	20.6	24.9	26.6
RONW (%)	23.1	21.1	19.4	23.4	25.2

Source: Company; Sharekhan estimates

Q3FY2023 Concall Highlights

- ◆ **Sales growth:** Sales growth was led by strong growth in the branded generics' market (70% of revenue) and steady performance in the generics business. Growth in branded generics was driven by new launch momentum, performance of the top brands, and integration of the acquired product portfolio.
- ◆ **Financial Performance:** There is a one-off item in the gross margin of 0.6% in the quarter due to under-absorption of the manufacturing costs as there was a temporary stoppage of manufacturing in October 2022 for 15-20 days for carrying out cleaning validation of certain equipment as a follow up to the USFDA audit.
- ◆ **Dividend:** The company's board approved an interim dividend of Rs. 14 per share.
- ◆ **India business:** Revenue grew at 17.4%, including Curatio's (acquired entity) revenue integrated. Torrent's growth in Q3FY2023 was at 12%, in line with 12% growth in India Pharmaceutical Market (IPM). Growth was aided by new launch performance, especially in the chronic segment, performance of its top brands, and strong growth of the Curatio portfolio. At the end of the quarter, the company has 19 brands in the top 500 of the IPM with over 13 brands having revenue of more than Rs. 100 crore of sales. Field force has been expanded further. MR count stands at 5,300, including Curatio's. Base business's MR strength stands at 4,700, which has also been expanded in the current quarter. The company expects India business to continue to fare well, backed by new product launches, top brands' performance, improving field force's productivity, and continued performance of the acquired companies' products, Curatio Healthcare.
- ◆ **Brazil:** Brazil is the biggest branded generic market for the company outside of India. Strong revenue growth was driven by equally strong growth in CNS products and the generic business, which contributes 14% to the Brazilian revenue. The company has launched six products over the past 12 months. The company plans to enhance the coverage of its CNS and cardio market share from 19% to 35.0% by 2025. The plan is on track as the company has received seven product approvals this year, while 10 products await approval. The company plans to file additional 10 new products by the end of this FY. IQVIA projects retail market growth of 11% in 2023 and 2024. The company expects to grow higher than the market growth.
- ◆ **Germany:** With the start of a new tender, won earlier in the year, and four new product launches in Q3FY2023, the company has been able to report growth in the segment. Management has guided for single-digit growth in the coming year based on the tender business wins, and around 10 new product launches likely by the end of FY2023. The new product launches will help it offset any pricing pressure.
- ◆ **U.S.:** The U.S. has received OAI for its Indrad, Gujarat, facility, whose capacity utilisation is 70%. For its Dahej and oncology facilities, whose capacity utilisation is in mid-50% levels, the company awaits the USFDA's inspection. Outlook in the U.S. depends on its ability to bring in new products in the market. The company plans to file 5-6 new products in FY2023. As of December 2022, 48 ANDAs were pending approvals from the USFDA. Generic is 14% of the revenue in the segment.
- ◆ **Outlook:** Brazil market will continue to lead growth and Germany should have a steady sequential recovery in the short-medium term.
- ◆ **India growth:** AIOCD growth for Torrent has been 12% y-o-y in Q3FY2023, volume growth has been 0.2%, pricing is 8.1% vs. 7.0% of IPM pricing growth, and new product launches have been at 3.5%. The company expects pricing growth in the 7-8% range is likely in the upcoming quarters as well. Key launches that have driven the pricing are Sitagliptin (no. 1 franchisee of the brand) and are likely to post in Rs. 4.8 crore to Rs. 5 crore of revenue monthly in it. Moreover, in the CNS space, pregabalin is doing well and retains the no. 1 market share. Since October 2022, the company has been realising cost savings in overlapping distribution, warehouse setups between it, and Curatio.
- ◆ **Debt:** Net debt should be Rs. 4,300 crore by the end of FY2023. Repayment of Rs. 1,200 crore is likely in FY2024; and in FY2025, a major chunk of cash flows will be utilised towards pre-payment of loans.
- ◆ **Capex:** Capex is expected to be Rs. 250-300 crore p.a.

Results (Consolidated)

Particulars	Rs cr				
	Q3FY23	Q3FY22	YoY %	Q2FY23	QoQ %
Total Sales	2,491.0	2,108.0	18.2	2,291.0	8.7
Expenditure	1,767.0	1,570.0	12.5	1,612.0	9.6
EBITDA	724.0	538.0	34.6	679.0	6.6
Depreciation	193.0	167.0	15.6	163.0	18.4
EBIT	531.0	371.0	43.1	516.0	2.9
Interest	102.0	62.0	64.5	69.0	47.8
Other income	-10.0	48.0	NM	16.0	NM
PBT	419.0	357.0	17.4	463.0	-9.5
Taxes	136.0	108.0	25.9	151.0	-9.9
PAT	283.0	249.0	13.7	312.0	-9.3
Reported Profit	283.0	249.0	13.7	312.0	-9.3
EPS (Rs.)	8.4	7.4	13.7	9.2	-9.3
Margins			BPS		BPS
EBITDA %	29.1	25.5	354	29.6	-57
EBIT %	21.3	17.6	372	22.5	-121
NPM%	11.4	11.8	-45	13.6	-226
Tax %	32.5	30.3	221	32.6	-16

Source: Company, Sharekhan Research

Region-wise revenue performance

Particulars	Rs cr		
	Q3FY23	Q3FY22	YoY %
India	1,259	1,072	17.4%
U.S.	291	235	23.8%
Germany	241	237	1.7%
Brazil	248	182	36.3%
Other countries (RoW)	291	227	28.2%
Others	160	155	3.2%
Total	2,490	2,108	18.1%

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Multiple growth engines ahead

The IPM is growing with increased consumer spend and awareness. Additionally, Indian pharmaceutical players with a large market share in IPM and a strong pipeline of speciality products will help them gain market share in the U.S. and thereby partially offset any impact of competitive pricing pressure in the U.S. Moreover, other factors such as faster product approvals and resolutions by the USFDA regards to plant observations 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, biosimilars, and injectables) and commissioning of expanded capacities by select players over the medium term. Collectively, this indicates a strong growth potential going ahead for Indian pharma companies.

■ Company outlook - Earnings prospects improve with strong outlook on India and Brazil

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 U.S., 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 U.S. 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. A timely and successful resolution of these USFDA observations at its two plants is critical and could result in earnings upgrades upon resolution.

■ Valuation - Maintain Buy with a revised PT of Rs. 1,788

Torrent's Q3 performance was mixed. However, the company expects Brazil market to continue to lead the growth and Germany should have steady sequential recovery in the short-medium term. The company expects India business also to continue to fare well, backed by new product launches, top brands' performance, improving field force's productivity, and continued performance of the acquired companies' products, Curatio Healthcare. However, outlook in the US appears subdued, as it depends on its ability to bring in new products in the market. The company plans to file 5-6 new products in FY2023. At the same time, as of December 2022, 48 ANDAs were pending approvals from the USFDA, while its Indrad and Dahej facilities are under OAI. At the CMP, the stock trades at 31.0x/24.2x its revised FY2024E/FY2025E EPS. Given the improved outlook on the earnings front, we maintain our rating on the stock to Buy with a revised price target (PT) of Rs. 1,788, as we value it at 28.2x its revised FY2025E EPS vs. 30.5x multiple used earlier, as the stock indicates an upside potential of 16% from its CMP.

Peer valuation

Companies	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)			EV/EBIDTA (x)			RoE (%)		
				FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Torrent Pharma	1537	33.8	52032.6	42.5	31.0	24.2	20.5	16.5	13.7	19.4	23.4	25.2
Cipla	1047.3	80.7	84502.6	30.4	24.8	20.8	18.3	15.8	13.2	13.7	14.7	15.2

Source: Company, Sharekhan estimates

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 U.S., 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. U.S. business is also stable. Two manufacturing plants of Torrent are reeling under regulatory issues with a warning letter being issued by the USFDA. Management expects 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 U.S. 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: BSE; Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Mirae Asset Global Investments	1.59
2	ICICI Prudential Life Insurance	1.24
3	Kotak Mahindra AMC	1.21
4	Vanguard Group Inc.	1.11
5	BlackRock Inc.	0.95
6	FMR LLC	0.91
7	Nippon Life India AMC	0.85
8	UTI Asset Management	0.84
9	Norges Bank	0.71
10	ICICI Prudential AMC	0.63

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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Compliance Officer: Ms. Binkle Oza; Tel: 022-61150000; email id: complianceofficer@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com.

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