

HOLD

TP: Rs 1,100 | ▲ 6%

SUN PHARMA

| Pharmaceuticals

| 01 November 2022

Strong Q2 but valuations full – cut to HOLD

- Brisk Q2 revenue growth at 14% YoY to Rs 110bn backed by ramp-up in global specialty business and healthy India/EM sales
- EBITDA margin up 375bps QoQ (110bps YoY) on a higher share of specialty products in the mix
- Valuations full post ~20% rally in the last 2M; downgrade from BUY to HOLD with TP unchanged at Rs 1,100

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Global specialty ramp-up remains key driver: SUNP reported strong 14% YoY growth in Q2FY23 revenue to Rs 110bn as the global specialty business clocked a 28% YoY (+5% QoQ) increase to US\$ 201mn on the back of Ilumya, Cequa and Winlevi sales. Overall US revenue declined 2% QoQ to US\$ 412mn.

India and EM sales healthy; currency volatility hits ROW: Product launches coupled with market share gains in existing products helped India business grow 8.5% YoY (+2% QoQ). SUNP did not record any revenue from Covid products in Q2FY23; adjusting for base-quarter Covid sales, India growth was at 10.9% YoY. Emerging markets grew 15% YoY (+10% QoQ), whereas currency volatility in ROW markets held growth back at a mere 4% YoY (-2% QoQ).

Better mix improves margins; R&D spend to accelerate: Robust growth in the specialty business coupled with likely inflow of production-linked incentives drove EBITDA margin gains of 375bps QoQ (110bps YoY) to 29.2%. Management has guided for acceleration in R&D activity but maintained guidance on spends at 6-8% of sales.

Earnings call highlights: (1) India salesforce expansion completed. (2) Momentum in Ilumya to continue. Psoriatic arthritis market smaller than psoriasis market for new indications. (3) Received PLI benefit in Q2. (4) Absolute increase in staff cost and other expenses on account of India salesforce expansion, Alchemy integration and higher selling & distribution expenses. (5) Total of 92 ANDAs (abbreviated new drug applications) and 13 NDAs (new drug applications) pending. (6) Forex loss in Q2FY23 was Rs. 2.4bn (vs. loss of Rs 764 in Q2FY22).

Downgrade to HOLD: The stock has rallied 20% over the past two months and is currently trading at valuations of 19.2x/17.6x FY23E/FY24E EV/EBITDA, which appear full. We retain our TP of Rs 1,100 based on an unchanged 18.5x FY24E EV/EBITDA multiple – a premium to the stock’s 5Y average of 17.5x. This offers just 6% upside potential and hence we downgrade our rating from BUY to HOLD.

Key changes

Target	Rating
◀ ▶	▼

Ticker/Price	SUNP IN/Rs 1,037
Market cap	US\$ 30.1bn
Free float	45%
3M ADV	US\$ 32.4mn
52wk high/low	Rs 1,049/Rs 734
Promoter/FPI/DII	54%/12%/22%

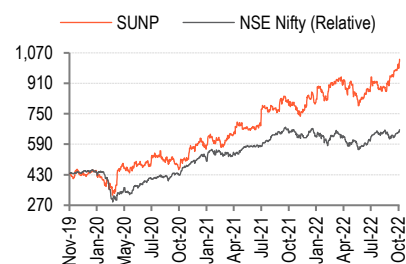
Source: NSE | Price as of 1 Nov 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	3,84,265	4,36,221	4,81,978
EBITDA (Rs mn)	1,02,395	1,22,169	1,31,628
Adj. net profit (Rs mn)	76,855	91,531	1,02,652
Adj. EPS (Rs)	32.0	38.2	42.8
Consensus EPS (Rs)	32.0	34.5	40.4
Adj. ROAE (%)	15.3	16.6	16.2
Adj. P/E (x)	32.4	27.2	24.2
EV/EBITDA (x)	23.2	19.2	17.4
Adj. EPS growth (%)	6.6	19.1	12.1

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)	H1FY23	H1FY22	YoY (%)
Net Sales	1,09,523	96,259	13.8	1,07,618	1.8	2,17,140	1,93,447	12.2
EBITDA	31,980	27,063	18.2	27,387	16.8	59,367	54,475	9.0
Depreciation	6,100	5,304	-	5,880	-	11,980	10,336	-
EBIT	25,881	21,759	18.9	21,507	20.3	47,388	44,139	7.4
Interest	194	360	-	137	-	331	710	-
Other Income	852	2,229	-	21	-	874	3,754	-
PBT	26,539	23,629	12.3	21,392	24.1	47,931	47,183	-
Less: Taxation	1,523	1,978	-	1,890	-	3,413	5,934	-
Less: Minority Interest	(21)	417	-	350	-	329	62	-
Recurring PAT	25,037	21,234	17.9	19,152	30.7	44,189	41,187	7.3
Exceptional items	(2,415)	(764)	-	1,457	-	(958)	(6,275)	-
Reported PAT	22,622	20,470	10.5	20,609	9.8	43,231	34,912	23.8
Key Ratios (%)			(bps)		(bps)			(bps)
Gross Margin	75.3	73.8	147	73.1	222	74.2	73.3	90
EBITDA Margin	29.2	28.1	109	25.4	375	27.3	28.2	(82)
Tax / PBT	5.7	8.4	-	8.8	-	7.1	12.6	-
NPM	22.9	22.1	-	17.8	-	20.4	21.3	-
EPS (Rs)	10.4	8.8	-	8.0	-	18.4	17.2	-

Source: Company, BOBCAPS Research

Fig 2 – Segmental performance

(Rs mn)	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)	H1FY23	H1FY22	YoY (%)
Formulation	1,02,658	90,582	13.3	99,897	2.8	2,02,555	1,81,399	11.7
Domestic	34,600	31,878	8.5	33,871	2.2	68,471	64,962	5.4
Exports	68,058	58,704	15.9	66,026	3.1	1,34,084	1,16,437	15.2
US	32,913	26,773	22.9	32,437	1.5	65,350	54,773	19.3
EM	20,704	18,005	15.0	18,911	9.5	39,615	34,058	16.3
ROW	14,441	13,926	3.7	14,678	(1.6)	29,119	27,606	5.5
APIs and others	5,434	4,985	9.0	6,543	(16.9)	11,977	10,863	10.2
OOI*	1,431	692	106.8	1,178	21.5	2,609	1,185	120.2
Net Sales	1,08,092	95,567	13.1	1,06,440	1.6	2,14,532	1,92,262	11.6
USDINR	79.8	74.1	7.7	77.2	3.5	78.5	73.9	6.2
US in \$ terms	412	361	14.1	420	(1.9)	833	741	12.3

Source: Company, BOBCAPS Research | *OOI – Other operating income

Valuation methodology

The stock has rallied 20% over the past two months and is currently trading at valuations of 19.2x/17.6x FY23E/FY24E EV/EBITDA, which appear full. We retain our TP of Rs 1,100 based on an unchanged 18.5x FY24E EV/EBITDA multiple, a premium to the stock's five-year average of 17.5x. This offers just 6% upside potential and hence we downgrade our rating from BUY to HOLD.

Fig 3 – Revised estimates

(Rs bn)	New		Old		Change (%)	
	FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
Revenue	436.2	482.0	430.4	473.1	1.4	1.9
EBITDA	122.2	131.6	118.0	132.0	3.6	(0.3)
EBITDA Margin (%)	28.0	27.3	27.4	27.9	60bps	(60bps)
EPS (Rs)	38.2	42.8	36.8	43.0	3.7	(0.6)

Source: BOBCAPS Research

Fig 4 – Key revenue assumptions

(Rs bn)	FY22E	FY23E	FY24E
India Formulations	127.6	142.9	157.2
US Formulations	113.7	131.4	141.8
EM/ROW Formulations	122.0	137.8	155.8
API & Others	21.0	24.1	27.2

Source: Company, BOBCAPS Research

Fig 5 – Peer comparison

Company	Ticker	Rating	Target Price (Rs)	Revenue CAGR FY22-24E (%)	EV/EBITDA(x)		ROCE (%)		Target P/E (x)
					FY22E	FY23E	FY22E	FY23E	
Dr. Reddy's	DRRD IN	HOLD	4,700	9.6	13.5	12.2	19.7	18.6	12.5
Lupin	LPC IN	SELL	600	15.9	14.0	10.7	9.3	13.0	10.0
Sun Pharma	SUNP IN	HOLD	1,100	13.4	19.0	17.6	18.3	17.8	18.5

Source: BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- earlier-than-expected launch of gRevlimid, and
- better pricing and lower competition in the base generics business.

Key downside risks are:

- regulatory hurdles/delays especially at the Halol plant,
- slow ramp-up in the specialty business, and
- above-expected price erosion in the US generics business.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Ajanta Pharma	AJP IN	2.1	1,323	1,500	BUY
Alembic Pharma	ALPM IN	1.4	578	770	HOLD
Alkem Labs	ALKEM IN	4.7	3,227	3,220	HOLD
Aurobindo Pharma	ARBP IN	3.9	550	695	BUY
Divi's Labs	DIVI IN	12.3	3,836	4,250	HOLD
Dr Reddy's Labs	DRRD IN	9.1	4,535	4,700	HOLD
Eris Lifesciences	ERIS IN	1.2	729	970	BUY
Glenmark Life Sciences	GLS IN	0.6	437	535	BUY
Laurus Labs	LAURUS IN	3.1	471	540	HOLD
Lupin	LPC IN	3.9	709	600	SELL
Sun Pharma	SUNP IN	30.1	1,037	1,100	HOLD

Source: BOBCAPS Research, NSE | Price as of 1 Nov 2022

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Total revenue	3,23,252	3,32,331	3,84,265	4,36,221	4,81,978
EBITDA	73,261	84,913	1,02,395	1,22,169	1,31,628
Depreciation	20,528	20,800	21,437	22,820	24,099
EBIT	52,734	64,113	80,958	99,349	1,07,529
Net interest inc./(exp.)	(3,027)	(1,414)	(1,274)	(1,303)	(1,226)
Other inc./(exp.)	6,360	8,355	9,215	12,257	16,714
Exceptional items	0	0	0	0	0
EBT	56,066	71,054	88,899	1,10,303	1,23,016
Income taxes	8,228	5,147	10,755	14,339	15,992
Extraordinary items	(2,606)	(43,061)	(44,129)	958	0
Min. int./Inc. from assoc.	4,219	(6,191)	1,289	4,432	4,372
Reported net profit	41,013	29,038	32,727	92,489	1,02,652
Adjustments	2,606	43,061	44,129	(958)	0
Adjusted net profit	43,620	72,099	76,855	91,531	1,02,652

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Accounts payables	40,937	39,737	44,793	46,308	49,197
Other current liabilities	29,746	54,349	34,472	34,504	34,539
Provisions	44,812	49,098	95,169	1,04,317	1,14,379
Debt funds	75,783	38,686	12,903	15,329	15,329
Other liabilities	0	0	0	0	0
Equity capital	2,399	2,399	2,399	2,399	2,399
Reserves & surplus	4,92,543	4,92,399	5,08,262	5,88,395	6,76,800
Shareholders' fund	4,94,942	4,94,798	5,10,661	5,90,794	6,79,199
Total liab. and equities	6,86,220	6,76,667	6,97,998	7,91,251	8,92,643
Cash and cash eq.	69,438	64,455	50,334	1,24,612	2,03,688
Accounts receivables	94,212	90,614	1,05,929	1,11,559	1,23,261
Inventories	78,750	89,970	89,968	1,02,134	1,12,847
Other current assets	1,02,583	1,04,305	85,817	85,817	85,817
Investments	1,01,431	96,125	1,28,486	1,28,486	1,28,486
Net fixed assets	1,04,808	1,02,350	1,03,713	1,04,893	1,04,794
CWIP	12,203	15,668	12,868	12,868	12,868
Intangible assets	1,22,795	1,13,180	1,20,884	1,20,884	1,20,884
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	6,86,220	6,76,667	6,97,998	7,91,251	8,92,643

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22A	FY23E	FY24E
Cash flow from operations	70,753	73,544	83,394	1,09,479	1,18,514
Capital expenditures	(25,524)	(12,192)	(27,704)	(24,000)	(24,000)
Change in investments	(22,407)	5,307	(32,361)	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(47,932)	(6,885)	(60,065)	(24,000)	(24,000)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(23,151)	(37,097)	(25,783)	2,426	0
Interest expenses	(3,027)	(1,414)	(1,274)	(1,303)	(1,226)
Dividends paid	(16,624)	(15,595)	(23,990)	(16,665)	(18,496)
Other financing cash flows	16,662	(17,535)	13,597	4,341	4,284
Cash flow from financing	(26,140)	(71,641)	(37,450)	(11,201)	(15,438)
Chg in cash & cash eq.	(3,318)	(4,983)	(14,121)	74,278	79,076
Closing cash & cash eq.	69,438	64,455	50,334	1,24,612	2,03,688

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22A	FY23E	FY24E
Reported EPS	17.1	12.1	13.6	38.6	42.8
Adjusted EPS	18.2	30.1	32.0	38.2	42.8
Dividend per share	6.9	6.5	10.0	6.9	7.7
Book value per share	190.2	193.7	200.1	231.7	266.8

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22A	FY23E	FY24E
EV/Sales	7.5	7.3	6.2	5.4	4.7
EV/EBITDA	33.1	28.4	23.2	19.2	17.4
Adjusted P/E	57.0	34.5	32.4	27.2	24.2
P/BV	5.4	5.4	5.2	4.5	3.9

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22A	FY23E	FY24E
Tax burden (Net profit/PBT)	77.8	101.5	86.5	83.0	83.4
Interest burden (PBT/EBIT)	106.3	110.8	109.8	111.0	114.4
EBIT margin (EBIT/Revenue)	16.3	19.3	21.1	22.8	22.3
Asset turnover (Rev./Avg TA)	12.1	12.2	14.0	14.6	14.3
Leverage (Avg TA/Avg Equity)	1.4	1.4	1.4	1.4	1.3
Adjusted ROAE	9.3	14.6	15.3	16.6	16.2

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22A	FY23E	FY24E
YoY growth (%)					
Revenue	12.7	2.8	15.6	13.5	10.5
EBITDA	20.7	15.9	20.6	19.3	7.7
Adjusted EPS	19.8	65.3	6.6	19.1	12.1
Profitability & Return ratios (%)					
EBITDA margin	22.7	25.6	26.6	28.0	27.3
EBIT margin	16.3	19.3	21.1	22.8	22.3
Adjusted profit margin	13.5	21.7	20.0	21.0	21.3
Adjusted ROAE	9.3	14.6	15.3	16.6	16.2
ROCE	8.2	13.2	14.6	16.3	15.8
Working capital days (days)					
Receivables	103	101	93	93	93
Inventory	89	93	85	85	85
Payables	163	169	149	149	149
Ratios (x)					
Gross asset turnover	1.2	1.2	1.3	1.3	1.4
Current ratio	3.0	2.4	1.9	2.3	2.7
Net interest coverage ratio	17.4	45.3	63.6	76.2	87.7
Adjusted debt/equity	(0.2)	(0.2)	(0.3)	(0.4)	(0.5)

Source: Company, BOBCAPS Research | Note: TA = Total Assets

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BUY – Expected return >+15%

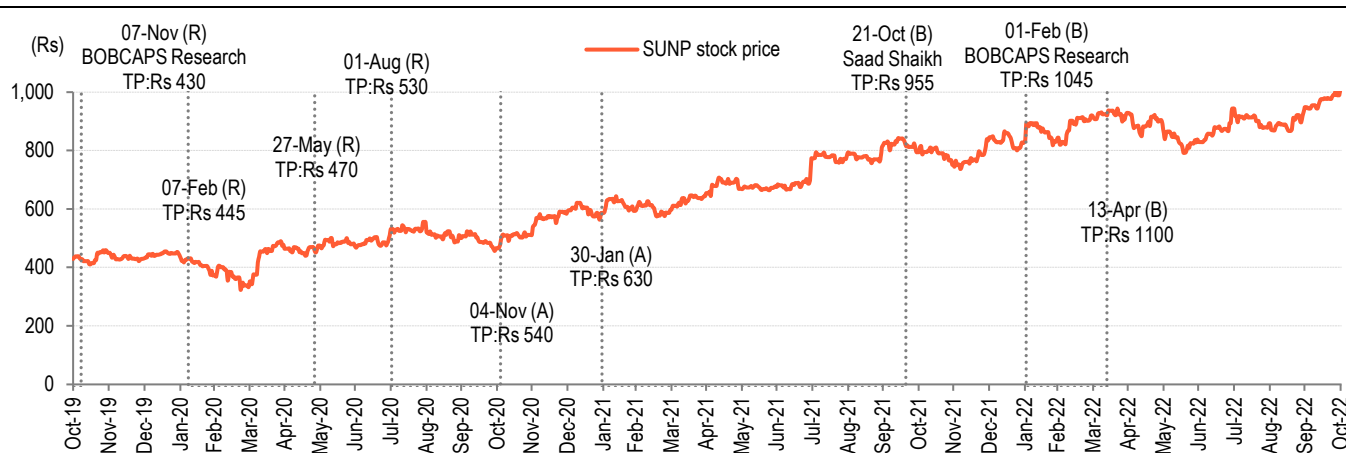
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): SUN PHARMA (SUNP IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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