



## India Infoline Result Update Sun Pharmaceutical Industries Ltd (Q3 FY07)

Rating: Maintain BUY CMP: Rs1,020 Target Price: Rs1,119  
January 31, 2007

Sun Pharma Industries Ltd (Sun) reported yet another consistent quarter with sales growing by 27.2% to Rs5.4bn and profitability growing by 35.9% to Rs2bn. Export formulations recorded a growth of 48% to Rs1.9bn with Caraco recording sales of US\$31.3mn for the quarter (51% growth yoy) with a profit of US\$10.1mn. Domestic formulations witnessed a growth of 18.5% to Rs2.9bn whereas for 9M FY07 it increased by 16.4% to Rs8.7bn. The market has grown at 18.5% for the quarter. Sun holds 3.2% market share as per the latest data. Margins have remained flat at 32.1% on account of higher material cost due to change in product mix and increase in R&D spending. PAT witnessed a growth of 36% to Rs2bn, translating into an annualized EPS of Rs41.9.

We remain positive on Sun's business prospects given its lean cost structure and specialty focus. Between Sun and Caraco, the combined entity has 61 ANDAs pending approval, 31 approvals (including 7 tentative approvals) which includes a mix of orals and injectables. The combined entity currently has 31 products in the US market. With focus on niche areas with specific technology, Sun has a strong pipeline of products to be launched over 2007-09. We estimate US sales to witness a CAGR of 38.1% to Rs9.7bn over FY06-09.

For the European market, Sun is looking at a partnership model approach rather than setting up its own front end. Sun's dominant position in niche and fast growing segments in the domestic market will enable it to grow faster than the industry and aid in achieving a 4% market share over the next two years. We estimate Sun to witness earnings CAGR of 24.4% to Rs11bn over FY06-09. At Rs1,020, the stock is trading at 27.5x FY07E EPS of Rs37.1, 22.6x FY08E EPS of Rs45.2 and 19.1x FY09E EPS of Rs53.3 on a fully diluted basis. We maintain BUY on the stock with a target price of Rs1,119 (21x FY09E) an upside of 8.1%. With a war chest of US\$500mn, an acquisition is round the corner, which holds potential upsides to our estimates. We believe Sun will target acquisition of a distressed asset and turn it around in three-four years time.

### Financial Highlights

Period to	Q3 FY07	Q3 FY06	growth	9M FY07	9M FY06	growth	FY07E	FY08E	FY09E
(Rs mn)			%			%			
Net Sales	5,401	4,247	27.2	15,879	12,301	29.1	21,698	26,625	31,868
Operating Profit	1,734	1,380	25.7	5,254	4,006	31.2	7,204	8,999	10,516
APAT	1,989	1,464	35.9	5,620	4,303	30.6	7,671	9,346	11,026
OPM (%)	32.1	32.5		33.1	32.6		33.2	33.8	33.0
FD EPS (Rs)	38.4	28.3		36.2	27.7		37.1	45.2	53.3
P/E (x)	26.5			28.2			27.5	22.6	19.1

### Q3 FY07 Result

#### Sales driven by export and domestic formulations

Sales for the quarter were driven by both export and domestic formulations. Export formulations witnessed a growth of 48% to Rs1.9bn. Caraco recorded sales of US\$31.1mn (51% yoy growth, 12% qoq growth) for the quarter with a profit of US\$10.1mn, despite significant pricing pressure. Sun and Caraco together have 31 products currently in the US market with 61 pending approval (including 7 tentative approvals). Domestic formulations sales also picked up after a not so exciting H1, growing at 18.5% to Rs2.94bn. The industry witnessed a growth of 18.5% for the quarter. Sun has a market share of 3.2% and is well placed to expand this share to 4% over the next two years.



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Table: Revenue breakup

Period to	Q3 FY07	Q3 FY06	Growth	9M FY07	9M FY06	Growth
Rs mn			(%)			(%)
<b>Domestic Market</b>	<b>3,168</b>	<b>2,663</b>	19.0	<b>9,421</b>	<b>8,136</b>	15.8
Formulation	2,935	2,476	18.5	8,687	7,464	16.4
Bulk	227	187	21.4	723	672	7.6
Others	6	0	-	11	0	-
<b>Exports Market</b>	<b>2,490</b>	<b>1,826</b>	36.4	<b>7,227</b>	<b>4,935</b>	46.4
Formulation	1,927	1,302	48.0	5,324	3,510	51.7
Bulk	556	524	6.1	1,883	1,425	32.1
Others	7	0	-	20	0	-
<b>Total</b>	<b>5,658</b>	<b>4,489</b>	26.0	<b>16,648</b>	<b>13,071</b>	27.4

### Margins remain flat on account of change in product mix and increase in R&D spending

Operating profit margin remained flat at 32.1% for Q3 FY07 mainly due to change in product mix as well as increase in R&D spending. R&D spending for the quarter increased by 230bps to 13.1% of sales. Flat margins could also be attributed to continued investments in Valeant and Able Labs, which are yet to contribute at the operating level. OPM is likely to expand to 33.8% over FY06-08.

With a war chest of US\$500mn, net interest and other income witnessed a growth of 75% to Rs635mn for Q3 FY07. Sun witnessed another quarter where tax outgo was positive. Effective tax rate is likely to remain at 2-3% over FY07-08. Consequently profitability witnessed a growth of 36% to Rs2bn, translating into an annualized EPS of Rs38.4 on a fully diluted basis. For 9M FY07, Sun recorded an annualized EPS of Rs36.2.

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