

Sun Pharmaceutical Industries

SUNP IN

Target price: **Rs561.00** → **Rs561.00**

Up/downside: **+15.8%**

Share price (20 Sep): **Rs484.40**

- 1 Buy (unchanged)
- 2 Outperform
- 3 Hold
- 4 Underperform
- 5 Sell

Domestic dominance continues

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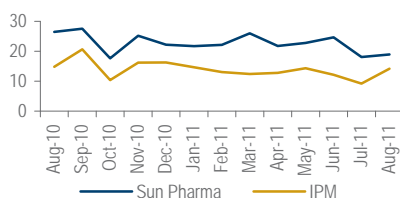
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- Leadership position in India's key specialist-chronic segments maintained
- Sitagliptin launched in India under Sun brand in 1H FY12
- Buy rating and Rs561 target price maintained

■ What's new

Following our recent visit to Sun Pharmaceutical Industries (Sun), we learned that unlike the other pharma companies in India, Sun has no plans to increase its sales force from the current 2,700. Sun is ranked fifth in terms of market share in India's pharma market (source: AIOCD-AWACS), despite having the smallest sales force among the top-10 Indian companies.

■ Sun: domestic sales YoY (%)



Source: Daiwa, AIOCD – AWACS

■ What's the impact

We believe Sun's ability to reach 100% of India's specialists is the key reason it has been able to maintain its dominance in the fast-growing

chronic-care segments. We believe Sun's tie-up with Merck (Not rated) in the India market for *Januvia/Janumet* is a good strategy to improve its presence in one of the fastest-expanding segments.

The tie-up involves marketing *Sitagliptin* under a different brand name (*Istavel/Istamet*) to diabetologists in India. For FY12, Sun has guided for total sales growth of 28-30% YoY. Meanwhile, with the recent resolution of the US FDA warning letter regarding its Cranbury site, we believe Sun's approval-filing rate will improve. It has seen its total domestic sales rise by more than 22% over the past six months, which is consistently higher than the India pharma market.

We forecast total sales and earnings CAGRs of 23.1% and 19.2%, respectively, for FY11-14, driven by the domestic-formulations business and an improvement in margins for the export business. Sun launched *Docetaxel* in 1Q FY12, and we assume there will be five generic companies in this market by the end of 1H FY12. Sun also received its first ANDA approval for the generic *Sumatriptan Autoinjector* in June 2011.

■ What we recommend

We maintain our Buy (1) rating for Sun as it has maintained its dominant position in the chronic-therapy segment in India, and given subsidiary Taro's (Not rated) improving operating performance. We maintain our SOTP-based six-month target price of Rs561, based on a target PER of 22x on our FY13 recurrent EPS forecast, plus Rs4/share for the *Para IV* upside potential and Rs39/share for cash. The key risks to our view would be greater-than-expected volatility at Taro's operations and a slower-than

expected expansion of the India pharma market.

■ How we differ

Our FY12 and FY13 EPS forecasts are respectively 3.9% and 6.3% higher than those of the Bloomberg consensus, due mainly to our higher EBITDA-margin forecasts.

Forecast revisions (%)

Year to 31 Mar	12E	13E	14E
Revenue change	0.0	0.0	0.0
Net-profit change	0.0	0.0	0.0
EPS change	0.0	0.0	0.0

Source: Daiwa forecasts

Share price performance



12-month range	375.37-525.65
Market cap (US\$bn)	10.44
Average daily turnover (US\$m)	10.56
Shares outstanding (m)	1,036
Major shareholder	Dilip Shanghi & Group (63.7%)

Financial summary (Rs)

Year to 31 Mar	12E	13E	14E
Revenue (m)	73,613	93,032	106,692
Operating profit (m)	20,490	25,524	29,165
Net profit (m)	22,089	26,944	30,748
Core EPS	21.327	26.015	29.687
EPS change (%)	21.7	22.0	14.1
Daiwa vs Cons. EPS (%)	3.9	6.3	8.9
PER (x)	22.7	18.6	16.3
Dividend yield (%)	0.8	1.0	1.2
DPS	4.000	5.000	6.000
PBR (x)	4.8	4.0	3.4
EV/EBITDA (x)	19.8	15.6	13.3
ROE (%)	23.1	23.5	22.4

Source: Bloomberg, Daiwa forecasts

Financial summary

■ **Key assumptions**

Year to 31 Mar	2007	2008	2009	2010	2011	2012E	2013E	2014E
Domestic sales growth YoY (%)	23.7	25.2	34.2	(6.0)	36.9	12.0	18.0	17.5
Taro Sales growth YoY (%)						108.4	9.8	3.0
Export sales growth YoY (%)	39.5	95.7	21.9	(11.3)	61.7	40.8	31.2	13.2

■ **Profit and loss (Rs m)**

Year to 31 Mar	2007	2008	2009	2010	2011	2012E	2013E	2014E
Domestic	11,144	13,954	18,733	17,605	24,096	26,994	31,853	37,427
Export	9,687	18,956	23,101	20,481	33,119	46,619	61,179	69,265
Others	0	0	0	0	0	0	0	0
Total revenue	20,831	32,909	41,833	38,086	57,214	73,613	93,032	106,692
Other income	0	0	0	1,988	0	0	0	0
COGS	(5,767)	(7,222)	(8,556)	(10,977)	(14,607)	(18,209)	(22,328)	(25,887)
SG&A	(3,205)	(4,280)	(8,138)	(9,373)	(13,319)	(15,987)	(20,932)	(24,006)
Other op. expenses	(5,948)	(6,865)	(7,733)	(7,624)	(11,630)	(18,927)	(24,248)	(27,634)
Operating profit	5,910	14,543	17,407	12,100	17,659	20,490	25,524	29,165
Net-interest inc./(exp.)	945	1,146	1,217	1,138	1,341	1,488	1,483	1,528
Assoc/forex/extraord./others	1,301	305	867	904	1,356	2,283	2,400	2,730
Pre-tax profit	8,157	15,994	19,491	14,142	20,355	24,262	29,408	33,423
Tax	0	(485)	(712)	(679)	(1,284)	(881)	(1,176)	(1,337)
Min. int./pref. div./others	(314)	(640)	(602)	48	(910)	(1,291)	(1,287)	(1,339)
Net profit (reported)	7,843	14,869	18,177	13,511	18,161	22,089	26,944	30,748
Net profit (adjusted)	7,665	14,869	18,176	13,504	18,158	22,089	26,944	30,748
EPS (reported) (Rs)	7.572	14.356	17.550	13.045	17.534	21.327	26.015	29.687
EPS (adjusted) (Rs)	7.400	14.356	17.549	13.038	17.531	21.327	26.015	29.687
EPS (adjusted fully-diluted) (Rs)	7.400	14.356	17.549	13.038	17.531	21.327	26.015	29.687
DPS (Rs)	1.350	2.100	2.750	2.750	3.500	4.000	5.000	6.000
EBIT	5,910	14,543	17,407	12,100	17,659	20,490	25,524	29,165
EBITDA	6,724	15,511	18,640	13,633	19,700	23,164	28,622	32,530

■ **Cash flow (Rs m)**

Year to 31 Mar	2007	2008	2009	2010	2011	2012E	2013E	2014E
Profit before tax	8,157	15,994	19,491	14,142	20,355	24,262	29,408	33,423
Depreciation and amortisation	813	969	1,233	1,533	2,041	2,674	3,098	3,365
Tax paid	(91)	(1,288)	(1,482)	(890)	(4,046)	(747)	(1,028)	(1,174)
Change in working capital	(5,358)	(7,572)	1,818	(4,675)	(533)	(4,168)	(7,397)	(5,236)
Other operational CF items	178	0	1	7	3	0	0	0
Cash flow from operations	3,699	8,102	21,060	10,117	17,819	22,021	24,081	30,378
Capex	(1,958)	(1,886)	(6,390)	(2,113)	(13,205)	(5,013)	(5,150)	(5,279)
Net (acquisitions)/disposals	0	0	0	0	0	0	0	0
Other investing CF items	998	(4,022)	(12,030)	(12,069)	8,354	(6,943)	(6,792)	(14,244)
Cash flow from investing	(960)	(5,908)	(18,420)	(14,182)	(4,851)	(11,956)	(11,942)	(19,524)
Change in debt	(7,601)	(9,722)	353	(77)	2,544	1,064	1,330	1,662
Net share issues/(repurchases)	38	69	0	0	0	0	0	0
Dividends paid	(1,482)	(2,547)	(3,332)	(3,321)	(4,213)	(4,847)	(6,059)	(7,271)
Other financing CF items	4,785	9,586	3,647	(3,155)	4,592	(1)	(1)	(1)
Cash flow from financing	(4,260)	(2,614)	668	(6,553)	2,923	(3,784)	(4,730)	(5,609)
Forex effect/others	(999)	4,022	12,030	12,069	(8,383)	6,943	6,792	14,245
Change in cash	(2,519)	3,602	15,338	1,451	7,509	13,225	14,202	19,490
Free cash flow	1,741	6,216	14,671	8,004	4,615	17,009	18,931	25,099

Source: Company, Daiwa forecasts

Financial summary continued ...
■ Balance sheet (Rs m)

As at 31 Mar	2007	2008	2009	2010	2011	2012E	2013E	2014E
Cash & short-term investment	16,345	19,947	35,285	36,737	44,246	57,471	71,672	91,162
Inventory	6,645	7,728	9,757	10,739	14,794	19,030	24,027	27,565
Accounts receivable	6,789	14,177	8,811	11,748	11,716	15,071	19,028	21,830
Other current assets	2,653	5,081	7,425	8,562	11,726	11,827	14,932	17,130
Total current assets	32,431	46,932	61,278	67,785	82,482	103,399	129,660	157,687
Fixed assets	10,122	11,040	16,196	16,776	27,940	30,279	32,331	34,245
Goodwill & intangibles	0	0	0	0	0	0	0	0
Other non-current assets	293	0	1,907	2,100	5,001	5,001	5,001	5,001
Total assets	42,846	57,972	79,381	86,661	115,423	138,678	166,991	196,933
Short-term debt	0	0	0	0	0	0	0	0
Accounts payable	2,966	3,722	3,767	4,095	9,203	11,839	14,947	17,148
Other current liabilities	80	2,651	3,431	3,484	5,030	5,919	7,474	8,574
Total current liabilities	3,046	6,373	7,198	7,579	14,234	17,758	22,421	25,722
Long-term debt	11,144	1,436	1,789	1,712	4,256	5,320	6,650	8,312
Other non-current liabilities	1,188	92	1,228	1,209	1,348	1,483	1,631	1,795
Total liabilities	15,378	7,901	10,215	10,500	19,838	24,561	30,702	35,829
Share capital	981	1,036	1,036	1,036	1,036	1,036	1,036	1,036
Reserves/R.E./others	26,050	47,150	66,160	73,193	86,078	103,319	124,204	147,680
Shareholders' equity	27,031	48,185	67,196	74,229	87,114	104,355	125,240	148,716
Minority interests	438	1,886	1,970	1,932	8,472	9,763	11,050	12,388
Total equity & liabilities	42,846	57,972	79,381	86,661	115,423	138,678	166,991	196,933
EV	496,944	485,082	470,181	468,614	470,188	459,319	447,734	431,246
Net debt/(cash)	(5,201)	(18,511)	(33,496)	(35,025)	(39,990)	(52,151)	(65,023)	(82,850)
BVPS (Rs)	26.085	46.523	64.878	71.668	84.108	101	121	144

■ Key ratios (%)

Year to 31 Mar	2007	2008	2009	2010	2011	2012E	2013E	2014E
Sales (YoY)	30.5	58.0	27.1	(9.0)	50.2	28.7	26.4	14.7
EBITDA (YoY)	37.0	130.7	20.2	(26.9)	44.5	17.6	23.6	13.7
Operating profit (YoY)	37.5	146.1	19.7	(30.5)	45.9	16.0	24.6	14.3
Net profit (YoY)	33.7	94.0	22.2	(25.7)	34.5	21.7	22.0	14.1
EPS (YoY)	33.7	94.0	22.2	(25.7)	34.5	21.7	22.0	14.1
Gross-profit margin	72.3	78.1	79.5	71.2	74.5	75.3	76.0	75.7
EBITDA margin	32.3	47.1	44.6	35.8	34.4	31.5	30.8	30.5
Operating-profit margin	28.4	44.2	41.6	31.8	30.9	27.8	27.4	27.3
ROAE	36.2	39.5	31.5	19.1	22.5	23.1	23.5	22.4
ROAA	18.7	29.5	26.5	16.3	18.0	17.4	17.6	16.9
ROCE	15.7	31.8	28.1	16.0	19.6	18.5	19.2	18.5
ROIC	29.7	51.5	50.3	30.6	35.9	35.8	38.8	39.2
Net debt to equity	net cash	net cash	net cash	net cash	net cash	net cash	net cash	net cash
Effective tax rate	0.0	3.0	3.7	4.8	6.3	3.6	4.0	4.0
Accounts receivable (days)	91.1	116.3	100.3	98.5	74.8	66.4	66.9	69.9
Payables (days)	45.9	37.1	32.7	37.7	42.4	52.2	52.5	54.9
Net interest cover (x)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Net dividend payout	17.8	14.6	15.7	21.1	20.0	18.8	19.2	20.2

Source: Company, Daiwa forecasts

■ Company profile

Sun Pharmaceutical was founded in 1983 by Dilip Shanghvi to manufacture formulations and bulk drugs. Initially operating a single plant at Vapi, Gujarat, it now has 17 manufacturing locations (including three in the US and one in Hungary). It is the industry leader in chronic care. Sun has expanded internally and via acquisitions, with an important acquisition being that of Caraco.

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