

Strong performance driven by one-off; downgrade to

July 29, 2010

HOLD

Price	Target Price
Rs1775	Rs1866
Sensex	17,992

Price Performance

(%)	1M	3M	6M	12M
Absolute	1	13	27	44
Rel. to Sensex	(0)	11	16	23

Source: Bloomberg

Stock Details

Sector	Pharmaceuticals
Reuters	SUN.BO
Bloomberg	SUNP@IN
Equity Capital (Rs mn)	1030
Face Value (Rs)	5
No of shares o/s (mn)	206
52 Week H/L (Rs)	1,846/1,118
Market Cap (Rs bn /USD mn)	372/7,957
Daily Avg Vol (No of shares)	226684
Daily Avg Turnover (US\$ mn)	8.0

Shareholding Pattern (%)

	J'10	M'10	D'09
Promoters	63.7	63.7	63.7
FII/NRI	19.7	20.4	20.2
Institutions	6.0	5.5	5.6
Private Corp	5.1	5.0	5.0
Public	5.6	5.4	5.5

Manoj Garg

manoj.garg@emkayglobal.com

+91 22 6612 1257

- Robust operating performance driven by higher than expected contribution from generic Eloxatin (one-off)
- Adjusting to one-off, recurring revenue, EBIDTA and PAT grew by 25%, 106% and 95% respectively driven by higher contribution of domestic formulation (low base)
- Recurring EPS for the quarter is Rs15.5
- Maintain base business earning estimates of Rs62.8/ Rs83 for FY11/12E; downgrade to Hold with price target of Rs1866

77% revenue growth driven by one-off in US and strong domestic growth

Sun Pharma reported strong revenue growth of 77% to Rs14bn driven by a) 153% growth in US subsidiary and b) 91% growth in domestic formulation business. Growth in the US subsidiary was largely driven by ~US\$85mn contribution from generic Eloxatin (limited competition; company has stopped distribution on 30th June as per court ruling) which had limited competition during the quarter. The growth in the domestic formulation business is driven by low base effect of Q1FY10. Adjusting to this, the growth in the domestic market was 17% to Rs5.98bn. Company continued to remain no 1 across 5 specialties in domestic market and has 3.7% market share in highly fragmented industry. International formulation (ex-Caraco) also reported 25% growth, however, due to special provision of US\$10mn, the reported no. for Export formulation (ex-Caraco) shows 20% decline. Management has maintained its revenue guidance of 18% growth in FY11E. We have projected 15% and 17% revenue growth in FY11E and FY12E respectively. Sun Pharma has also announced that US appeal court has ruled in their favor for Gemzar patent case (US\$700mn revenue; Teva has FTF status; apart from Sun and Teva, there are two more filer).

Revenue mix

	Q1FY11	Q1FY10	Grwth	Q4FY10	QoQ Gr.(%)
Domestic	6323.6	3411.2	85%	5312.3	19%
Formulations	5984.2	3128.7	91%	5136.2	17%
Bulk	335.1	278.7	20%	169.8	97%
Others	4.3	0.38	1032%	6.3	-32%
Exports	7886.3	4603	71%	4944.9	59%
Formulations	6782	3404	99%	3910.6	73%
Caraco	59280	2341	2432%	2558.0	2217%
Ex Caraco	854	1063	-20%	1353	-37%
Bulk	1103.5	1190	-7%	995.6	11%
Others	0.8	9	-91%	38.7	-98%
Total	14209.9	8014	77%	11092	28%

Financials

YE-	Net	EBITDA		EPS	EPS	RoE	EV/			
Mar	Sales	(Core)	(%)	APAT	(Rs)	% chg	P/E	EBITDA	P/BV	
FY09	41,870	18,676	44.6	18,178	87.8	22.3	31.2	20.6	19.2	5.3
FY10	41,028	13,628	33.2	12,590	60.8	(30.7)	17.7	27.7	25.8	4.6
FY11E	47,075	15,751	33.5	14,905	72.0	18.4	17.5	25.1	21.8	4.0
FY12E	54,917	18,038	32.8	17,456	84.3	17.1	17.8	21.4	18.4	3.5

EBIDTA margins of 44% driven by higher one-off sales and favorable product mix

EBIDTA for the quarter was up by 375% (OPM of 44%) to Rs6.2bn driven by contribution from one-off sales and higher contribution from domestic formulation business. Adjusting to one time contribution from Eloxatin, the recurring EBIDTA for the quarter is Rs2.75bn (OPM of 28%). Overall, company has witnessed 29% and 18% increase in RM cost and other expenditures, however, employee cost remain flat at Rs1.25bn. We have estimated recurring EBIDTA of 30.5% for FY11E.

APAT was up by 244% to Rs5.6bn

Despite lower other income (down 81% YoY) on account of lower interest income and forex loss of Rs88mn, the APAT was up by 244% to Rs5.64bn. It is higher than our estimates of Rs4.2bn mainly because of higher than expected contribution from generic Eloxatin sales. Adjusting to generic Eloxatin contribution, the recurring PAT is Rs3.2bn (EPS of Rs15.5). Our full year estimates for recurring earnings are Rs62.8 and Rs83.

Maintain earning estimates and downgrade to Hold

We maintain our base business earning estimates of Rs62.8 and Rs83 for FY11E and FY12E respectively. Since our previous note dated May25, 2010, the stock has given 16% absolute return and 11% relative return to Sensex. Though we still believe that worst is behind us and expect robust earning growth in the base business (32% CAGR over FY10-12E) driven by a) 20% CAGR in domestic formulation business, b) 35% CAGR in international formulation business (ex-Caraco) and c) resolution of FDA issue at Caraco and increased contribution of controlled substances product portfolio. However, we are of the view that valuations are already rich (21x FY12E recurring earning; adjusting to NPV of Rs40 for Para IV pipeline) and provides limited upside opportunity. Roll-over target price on FY12E and raise it to Rs1866 (22x FY12E and Rs40 as NPV of Para IV). However downgrade the rating from Buy to Hold.

Quarterly Financials

Rs mn	Q1FY10	Q2FY10	Q3FY10	Q4FY10	Q1FY11	YoY (%)	QoQ (%)
Revenue	7,885	10,889	10,209	11,092	13,997	77.5	26.2
Expenditure	6,590	7,379	6,525	6,907	7,837	18.9	13.5
<i>as % of sales</i>	<i>83.6</i>	<i>67.8</i>	<i>63.9</i>	<i>62.3</i>	<i>56.0</i>		
Consumption of RM	2,602	2,858	2,857	2,662	3,357	29.0	26.1
<i>as % of sales</i>	<i>33.0</i>	<i>26.2</i>	<i>28.0</i>	<i>24.0</i>	<i>24.0</i>		
Employee Cost	1,251	1,249	1,163	1,160	1,246	(0.4)	7.4
<i>as % of sales</i>	<i>15.9</i>	<i>11.5</i>	<i>11.4</i>	<i>10.5</i>	<i>8.9</i>		
Other expenditure	2,737	3,272	2,505	3,085	3,235	18.2	4.8
<i>as % of sales</i>	<i>34.7</i>	<i>30.0</i>	<i>24.5</i>	<i>27.8</i>	<i>23.1</i>		
EBITDA	1,295	3,510	3,684	4,185	6,160	375.7	47.2
Depreciation	376	379	359	419	402	7.0	(4.1)
EBIT	919	3,131	3,325	3,766	5,758	526.5	52.9
Other Income	603	988	228	138	115	(80.9)	(16.4)
Interest							
PBT	1,522	4,119	3,553	3,903	5,873	285.8	50.5
Total Tax	40	400	261	(12)	97	141.9	(882.3)
Adjusted PAT	1,482	3,720	3,293	3,916	5,776	289.7	47.5
Minority Interest	-156	145	0	-8	133.1		
APAT after MI	1,638	3,575	3,293	3,924	5,643	244.4	43.8
Extra ordinary items	0	0	0	0	0		
Reported PAT	1,638	3,575	3,293	3,924	5,643	244.4	43.8
Reported EPS	7.2	22.6	15.9	18.9	27.2	280.7	44.1

Margins (%)						(bps)	(bps)
EBIDTA	16.4	32.2	36.1	37.7	44.0	(150)	850
EBIT	11.7	28.8	32.6	33.9	41.1	70	720
EBT	19.3	37.8	34.8	35.2	42.0	250	680
PAT	20.8	32.8	32.3	35.4	40.3	590	750
Effective Tax rate	2.6	9.7	7.3	(0.3)	1.7		

Key Financial

Income Statement

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Net Sales	41,870	41,028	47,075	54,917
<i>Growth (%)</i>	27.1	-2.0	14.7	16.7
Expenditure	23,194	27,400	31,324	36,879
Raw Materials	8,556	10,978	13,218	15,520
SGA	9,354	0	10,103	12,216
Employee Cost	3,401	4,822	5,401	6,211
Other Exp	1,882	11,599	2,602	2,932
EBITDA	18,676	13,628	15,751	18,038
<i>Growth (%)</i>	20.2	-27.0	15.6	14.5
EBITDA margin (%)	44.6	33.2	33.5	32.8
Depreciation	1,233	1,533	1,689	1,814
EBIT	17,443	12,095	14,062	16,224
EBIT margin (%)	41.7	29.5	29.9	29.5
Other Income	2,049	915	2,372	3,023
Interest expenses	0	-1,139	0	0
PBT	19,492	14,148	16,434	19,247
Tax	712	679	1,068	1,251
<i>Effective tax rate (%)</i>	3.7	4.8	6.5	6.5
Adjusted PAT	17,575	12,631	14,444	16,916
(Profit)/loss from JV's/Ass/MI	-603	41	-461	-540
Adjusted PAT after MI	18,178	12,590	14,905	17,456
<i>Growth (%)</i>	22.3	-30.7	18.4	17.1
Net Margin (%)	43.4	30.7	31.7	31.8
E/O items	0	0	0	0
Reported PAT	18,178	13,511	14,905	17,456
<i>Growth (%)</i>	22.3	-25.7	10.3	17.1

Cash Flow

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
PBT (Ex-Other income)	17,443	13,234	14,062	16,224
Depreciation	1,233	1,533	1,689	1,814
Interest Provided	0	-1,139	0	0
Other Non-Cash items	0	0	0	0
Chg in working cap	1,816	-3,240	-3,241	-4,376
Tax paid	0	0	0	0
Operating Cashflow	20,492	10,388	12,510	13,661
Capital expenditure	-7,914	-2,469	-2,000	-2,000
Free Cash Flow	12,578	7,919	10,510	11,661
Other income	2,049	915	2,372	3,023
Investments	-11,035	0	0	0
Investing Cashflow	-16,900	-1,555	372	1,023
Equity Capital Raised	0	0	0	0
Loans Taken / (Repaid)	353	-500	-500	0
Interest Paid	0	1,139	0	0
Dividend paid (incl tax)	-3,215	-2,364	-2,697	-3,158
Income from investments	0	0	0	0
Others	4,764	0	0	0
Financing Cashflow	1,902	-1,725	-3,197	-3,158
Net chg in cash	4,302	6,430	8,617	10,275
Opening cash position	12,389	16,690	23,120	31,738
Closing cash position	16,690	23,120	31,738	42,013

Balance Sheet

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Equity share capital	1,036	1,036	1,036	1,036
Reserves & surplus	69,414	80,560	92,769	107,066
Net worth	70,449	81,596	93,804	108,102
Minority Interest	1,970	1,929	2,390	2,930
Secured Loans	227	227	227	227
Unsecured Loans	1,562	1,062	562	562
Loan Funds	1,789	1,289	789	789
Net deferred tax liability	-679	-679	-679	-679
Total Liabilities	73,530	84,135	96,304	111,142
Gross Block	24,730	28,301	30,301	32,301
Less: Depreciation	6,851	8,415	10,104	11,917
Net block	17,879	19,886	20,197	20,383
Capital work in progress	1,571	500	500	500
Investment	18,595	18,595	18,595	18,595
Current Assets	42,683	52,619	65,605	81,554
Inventories	9,757	9,847	11,289	13,171
Sundry debtors	8,811	12,308	14,112	16,464
Cash & bank balance	16,690	23,120	31,738	42,013
Loans & advances	7,425	7,344	8,467	9,906
Other current assets	0	0	0	0
Current lia & Prov	7,198	7,465	8,593	9,890
Current liabilities	3,767	4,908	5,680	6,483
Provisions	3,431	2,557	2,913	3,407
Net current assets	35,485	45,155	57,012	71,664
Misc. exp & Def. Assets	0	0	0	0
Total Assets	73,530	84,135	96,304	111,142

Key Ratios

Y/E, Mar	FY09	FY10	FY11E	FY12E
Profitability (%)				
EBITDA Margin	44.6	33.2	33.5	32.8
Net Margin	43.4	30.7	31.7	31.8
ROCE	27	15	15	16
ROE	31	18	18	18
RoIC	0.0	0.0	0.0	0.0
Per Share Data (Rs)				
EPS	87.8	60.8	72.0	84.3
CEPS	70.4	51.3	71.0	91.7
BVPS	340.1	394.0	452.9	521.9
DPS	27.5	19.5	22.3	26.1
Valuations (x)				
PER	20.6	27.7	25.1	21.4
P/CEPS	25.7	35.2	25.4	19.7
P/BV	5.3	4.6	4.0	3.5
EV / Sales	8.6	8.6	7.3	6.1
EV / EBITDA	19.2	25.8	21.8	18.4
Dividend Yield (%)	1.5	1.1	1.2	1.4
Gearing Ratio (x)				
Net Debt/ Equity	-0.2	-0.3	-0.3	-0.4
Net Debt/EBIDTA	-0.8	-1.6	-2.0	-2.3
Working Cap Cycle (days)	194	219	219	220

Recommendation History: Sun Pharma – SUNP IN

Date	Reports	Reco	CMP	Target
25.05.2010	Sun Pharma Q4FY10 Result Update	Buy	1,550	1,730
26.04.2010	Sun Pharma Event Update	Hold	1,684	1,632
31.07.2009	Sun Pharma Q1FY10 Result Update	Not Rated	1,145	NA

Recent Research Reports

Date	Reports	Reco	CMP	Target
29.07.2010	Lupin Pharma Q1FY11 Result Update	Accumulate	1,920	2,111
28.07.2010	Jubilant Organosys Q1FY11 Result Update	Buy	352	455
28.07.2010	Glenmark Pharma Q1FY11 Result Update	Hold	285	308
27.07.2010	Cadila Healthcare Q1FY11 Result Update	Buy	645	720

Emkay Global Financial Services Ltd.

Paragon Center, H -13 -16, 1st Floor, Pandurang Budhkar Marg, Worli, Mumbai – 400 013. Tel No. 6612 1212. Fax: 6624 2410

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