

## ACCUMULATE

CMP*	Rs555
Target Price	Rs580

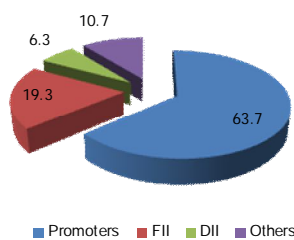
## Stock Info

Sector	Pharmaceuticals
Market Cap (Rs cr)	57,440
52 Week High/Low	603/404
Avg. Daily Volume (3m, '000)	88.3
Avg. Daily Value (3m, cr)	46.1
Dividend Yield (%)	0.6
Sensex	17,849
Nifty	5,416
BSE Code	524715
NSE Code	SUNPHARMA

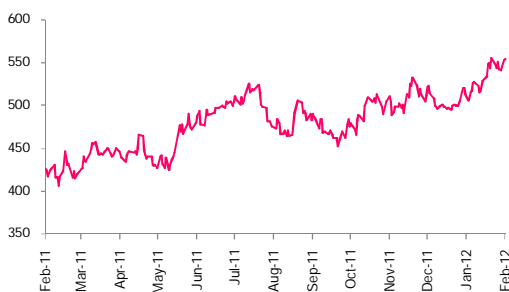
## Stock Performance

(%)	SUN PHARMA	NIFTY
1-week	2.0	1.5
1-month	9.7	11.3
1-year	30.2	(0.7)

## Shareholding Pattern (%)



## Stock Price Chart



Note: \*CMP as on February 14, 2012

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## Taro continues to be the key growth driver

## Key highlights of the result

- Taro boosts sales:** Sun Pharma's top-line for 3QFY2012 grew at 37.4% yoy, largely driven by Taro (31% of the total sales) and favorable currency. The domestic formulations (up 14% yoy), adjusting for the discontinued third party manufacturing, the underlying business grew 17% yoy. The US formulations grew by a staggering 63.1% yoy on a high base of 3QFY2011 (due to inclusion of high margin Eloxatin), boosted by Taro (aided by price increase in select products, largely non-recurring sales in nature). API grew by 39% in 3QFY2012.
- EBITDA highest in last 3 years:** The gross margins expanded by 1,000bp to 82.4%, aided by inventory valuation impact due to depreciating rupee. However, the same may not be sustainable going forward. The operating margins improved substantially at 44.9% (highest in last 3 years) on account of strong operating performance from Taro. Taro's OPM for the quarter stood at a strong 50.3%. Owing to lower tax rate the RPAT stood at -Rs668.3cr (up 91% yoy).
- Concall takeaways:** (1) The management, has upgraded its top-line guidance to 32-34% for FY2012 (earlier 28-30%), (2) Taro's PAT was restricted by forex loss of US\$6.3mn, (3) Taro's higher growth and margin momentum were led by price hikes (flat volume growth) in certain dermatology products in US, (4) R&D expenses to stay higher at ~6% of sales and tax rate at ~9% largely on account of Taro, (5) Management has maintained status quo on Caraco update, while the Taro buyout decision is awaited from its shareholders, (6) Sun filed 1 ANDA in 3QFY2012 and has 148 ANDAs pending for approval, and (7) Capex for FY2012 stands at Rs400cr, while cash on books is ~Rs1bn.

## Outlook and Valuation

Sun Pharma delivered results which were above our expectations in 3QFY2012, owing to robust performance from Taro's dermatology portfolio and rupee depreciation. However, with most of Taro's growth coming from price increases, we believe that volume growth is likely to be a challenge going ahead. Nevertheless, with strong para IV pipeline in US and gradual improvement in the domestic business, the growth prospects of the company appear promising.

Factoring in the strong performance and revised guidance, we upgrade our estimates for FY2012E and FY2013E. Our revised EPS stands at Rs21.8 (Rs21 earlier) and Rs26.4 (Rs24.4 earlier) for FY2012E and FY2013E respectively. Apt utilization of cash could boost the return ratios. Sun is currently trading at 25.4x and 21x its FY2012E and FY2013E EPS respectively. **We maintain Accumulate on the stock with the revised price target of Rs580 (earlier Rs562, achieved on 6<sup>th</sup> Feb 2012).**

## Risks to the view

- Delay in product approvals and higher than expected liability on Protonix litigation
- Lower than expected performance from Taro

Year End	Net Revenues		EBITDA		Net income (adjusted)		RoE	RoCE	EPS	Valuations (X)	
	(Rs cr)	% growth	(Rs cr)	% margin	(Rs cr)	% growth	%	%	(Rs)	P/E	EV/EBITDA
FY2010	4,103	(4.0)	1,363	33.2	1,351	(25.7)	17.3	17.7	13.0	42.5	40.7
FY2011	5,721	39.5	1,967	34.4	1,816	34.4	19.1	20.5	17.5	31.6	28.2
FY2012E	7,637	33.5	2,986	39.1	2,258	24.3	19.3	24.3	21.8	25.4	18.4
FY2013E	8,852	15.9	3,523	39.8	2,729	20.9	19.0	23.4	26.4	21.0	15.0

**Exhibit 1: Quarterly performance (Consolidated)**

Particulars (Rs cr)	3QFY12	3QFY11	% yoy	2QFY12	% qoq	9MFY12	9MFY11	% yoy
<b>Net sales</b>	<b>2,145.1</b>	<b>1,561.7</b>	<b>37.4</b>	<b>1,894.6</b>	<b>13.2</b>	<b>5,675.5</b>	<b>4,258.2</b>	<b>33.3</b>
Material cost	378.1	432.4	(12.6)	363.9	3.9	1,149.0	1,147.5	0.1
% of net sales	17.6	27.7		19.2		20.2	26.9	
Staff costs	288.5	275.4	4.8	272.7	5.8	839.8	545.6	53.9
% of net sales	13.4	17.6		14.4		14.8	12.8	
R&D Expenses	106.9	89.6	19.3	89.1	20.0	284.5	217.6	
% of net sales	5.0	5.7		4.7		5.0	5.1	
Other expenses	407.9	323.8	26.0	384.9	6.0	1,106.9	824.0	34.3
% of net sales	19.0	20.7		20.3		19.5	19.4	
<b>Total operating expenditure</b>	<b>1,181.4</b>	<b>1,121.2</b>	<b>5.4</b>	<b>1,110.6</b>	<b>6.4</b>	<b>3,380.2</b>	<b>2,734.6</b>	<b>23.6</b>
Operating profit	963.8	440.5	118.8	784.0	22.9	2,295.3	1,523.5	50.7
OPM (%)	44.9	28.2		41.4		40.4	35.8	
Interest	0.0	0.0	-	0.0	-	0.0	0.0	-
Depreciation	77.4	80.5	(3.8)	66.8	16.0	208.9	155.9	34.0
<b>EBIT</b>	<b>886.4</b>	<b>360.1</b>	<b>146.2</b>	<b>717.3</b>	<b>23.6</b>	<b>2,086.4</b>	<b>1,367.7</b>	<b>52.5</b>
Other Income	(27.2)	58.0	(146.9)	118.3	(123.0)	187.9	161.9	16.0
<b>PBT</b>	<b>859.1</b>	<b>418.1</b>	<b>105.5</b>	<b>835.5</b>	<b>2.8</b>	<b>2,274.2</b>	<b>1,529.6</b>	<b>48.7</b>
Total tax	63.4	54.5	16.4	128.1	(50.5)	205.8	81.4	152.9
Tax Rate (%)	7.4	13.0		15.3		9.0	5.3	
Minority Interest	127.4	13.4	847.8	109.7	16.1	301.4	30.1	900.7
<b>Adjusted PAT</b>	<b>668.3</b>	<b>350.2</b>	<b>90.9</b>	<b>597.7</b>	<b>11.8</b>	<b>1,767.0</b>	<b>1,418.1</b>	<b>24.6</b>
Net profit margin (%)	31.2	22.4		31.5		31.1	33.3	
Extra-ordinary Items	0.0	0.0	-	0.0		0.0	0.0	-
Forex loss/(gain)	0.0	0.0	-	0.0		0.0	0.0	-
Others	0.0	0.0	-	0.0		0.0	0.0	-
<b>Reported Net profit</b>	<b>668.3</b>	<b>350.2</b>	<b>90.9</b>	<b>597.7</b>	<b>11.8</b>	<b>1,767.0</b>	<b>1,418.1</b>	<b>24.6</b>
<b>Reported EPS (Rs)</b>	<b>6.5</b>	<b>3.4</b>		<b>5.8</b>		<b>17.1</b>	<b>13.7</b>	

Source: Company, RSec Research

Taro's dermatology portfolio has witnessed strong market share gains; certain product sales are one-off in nature

**Taro:** Taro reported 44.9% yoy growth (in US\$ terms) in 3QFY2012 to US\$148.1mn with a healthy bottom-line of US\$62.4mn. The operating margins skyrocketed to 50.3%, highest in last 8 quarters. However, the sales were largely driven by value growth (flat in volume growth). The Taro management has indicated that the R&D expenses will get normalized for the full year and return to the same levels of FY2011 at 9% (note that the R&D expenses were 5.8% for the current quarter). Further, the management has also indicated that they are likely to witness pricing pressures in few products due to increasing competition and that the sales of such products are non-recurring in nature.

**Caraco:** The ongoing issues with USFDA are yet to be resolved. The management maintains a status quo on the same.

**Exhibit 2: Segment wise revenue break-up**

Particulars (Rs cr)	3QFY12	3QFY11	% yoy	2QFY11	% qoq
Domestic Formulations	695.6	610.2	14.0	704.6	(1.3)
Exports	1,321.0	858.9	53.8	1,055.8	25.1
US Formulations	1,040.0	637.6	63.1	799.1	30.1
ROW Formulations	281.0	221.3	27.0	256.7	9.4
Bulk	153.6	113.6	35.2	160.3	(4.2)
Others	1.7	0.4	324.4	0.4	324.4
<b>Total Gross Sales</b>	<b>2,172.0</b>	<b>1,583.1</b>	<b>37.2</b>	<b>1,921.1</b>	<b>13.1</b>

*Focus on chronic therapies continue to drive domestic formulations*

**Indian Formulations:** The domestic markets grew 14% during the quarter, as Sun Pharma discontinued its third party manufacturing business. However, adjusting on a like to like basis, the growth has been healthy at 17% yoy. Sun launched 6 new products in 3QFY2012, taking it to a total of 20 launches in 9MFY2012. The company expects to maintain its growth rate, driven by new product launches and has guided for ~30 products to be launched in FY2012. It remains progressive on its chronic therapies and has identified them as the growth drivers for the Indian market.

The JV with Merck has been progressing well and Sun has attained 10% market share of Sitagliptin launched recently in the Indian market.

**Emerging markets:** The RoW market grew by an astounding 27% during the quarter (on a higher base), which is commendable. The growth was largely contributed by Taro's sales in the emerging markets, excluding which the underlying growth stands at 20%+ yoy.

### Outlook and Valuation

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Factoring in the strong performance and revised guidance, we upgrade our estimates for FY2012E and FY2013E. Our revised EPS stands at Rs21.8 (Rs21 earlier) and Rs26.4 (Rs24.4 earlier) for FY2012E and FY2013E respectively. Apt utilization of cash could boost the return ratios. Sun is currently trading at 25.4x and 21x its FY2012E and FY2013E EPS respectively. **We maintain Accumulate on the stock with the revised price target of Rs580 (earlier Rs562, achieved on 6<sup>th</sup> Feb 2012).**

**Profit & Loss Statement**

Y/E March (Rs cr)	FY2010	FY2011	FY2012E	FY2013E
<b>Gross sales</b>	<b>4,180</b>	<b>5,807</b>	<b>7,739</b>	<b>8,972</b>
Less: Excise duty	78	85	102	120
Net Sales	4,103	5,721	7,637	8,852
<b>Total Expenditure</b>	<b>2,739</b>	<b>3,754</b>	<b>4,651</b>	<b>5,329</b>
Cost of Materials	1,193	1,461	1,604	1,815
R&D Expense	208	308	428	531
Personnel	401	800	1,092	1,213
Others	937	1,186	1,527	1,770
<b>EBITDA</b>	<b>1,363</b>	<b>1,967</b>	<b>2,986</b>	<b>3,523</b>
% chg	(26.9)	44.3	51.6	18.0
(% of Net Sales)	33.2	34.4	39.1	39.8
Depre. & Amortization	153	204	275	294
<b>EBIT</b>	<b>1,210</b>	<b>1,763</b>	<b>2,711</b>	<b>3,229</b>
% chg	(30.5)	45.7	53.5	19.1
(% of Net Sales)	29.5	30.8	35.5	36.5
Interest & other Charges	0	0	0	0
Other Income	205	273	210	210
(% of PBT)	14.5	13.4	7.2	6.1
<b>Recurring PBT</b>	<b>1,415</b>	<b>2,036</b>	<b>2,921</b>	<b>3,439</b>
% chg	(27.4)	43.9	43.5	17.7
<b>PBT (reported)</b>	<b>1,415</b>	<b>2,036</b>	<b>2,921</b>	<b>3,439</b>
Tax	68	128	263	310
(% of PBT)	4.8	6.3	9.0	9.0
Minority Interest	(4.1)	91.3	400.0	400.0
<b>PAT (reported)</b>	<b>1,351</b>	<b>1,816</b>	<b>2,258</b>	<b>2,729</b>
<b>PAT after MI (reported)</b>	<b>1,351</b>	<b>1,816</b>	<b>2,258</b>	<b>2,729</b>
<b>ADJ. PAT</b>	<b>1,351</b>	<b>1,816</b>	<b>2,258</b>	<b>2,729</b>
% chg	(25.7)	34.4	24.3	20.9
(% of Net Sales)	32.9	31.7	29.6	30.8
<b>Basic EPS (Rs)</b>	<b>13.0</b>	<b>17.5</b>	<b>21.8</b>	<b>26.4</b>
<b>Fully Diluted EPS (Rs)</b>	<b>13.0</b>	<b>17.5</b>	<b>21.8</b>	<b>26.4</b>
% chg	(85.1)	34.4	24.3	20.9

**Cash Flow Statement**

Y/E March (Rs cr)	FY2010	FY2011	FY2012E	FY2013E
Profit before tax	1,415	2,036	2,921	3,439
Depreciation	153	204	275	294
Change in Working Capital	466	55	1,457	907
Interest / Dividend (Net)	0	0	0	0
Direct taxes paid	68	128	263	310
Others	(1,353)	(53)	(362)	(410)
<b>Cash Flow from Operations</b>	<b>(183)</b>	<b>2,260</b>	<b>1,640</b>	<b>2,726</b>
(Inc.)/ Dec. in Fixed Assets	186	2,218	450	350
(Inc.)/ Dec. in Investments	1,307	(935)	-	-
<b>Cash Flow from Investing</b>	<b>(1,493)</b>	<b>(1,283)</b>	<b>(450)</b>	<b>(350)</b>
Issue of Equity	-	-	-	-
Inc./(Dec.) in loans	849	1,128	(80)	(50)
Dividend Paid (Incl. Tax)	332	421	423	423
Interest / Dividend (Net)	0	0	0	0
<b>Cash Flow from Financing</b>	<b>517</b>	<b>707</b>	<b>(503)</b>	<b>(473)</b>
Inc./(Dec.) in Cash	(1,159)	1,685	687	1,903
<b>Opening Cash balances</b>	<b>1,669</b>	<b>509</b>	<b>2,193</b>	<b>2,880</b>
<b>Closing Cash balances</b>	<b>509</b>	<b>2,194</b>	<b>2,880</b>	<b>4,784</b>

**Balance Sheet**

Y/E March (Rs cr)	FY2010	FY2011	FY2012E	FY2013E
<b>SOURCES OF FUNDS</b>				
Equity Share Capital	104	104	104	104
Preference Capital	-	-	-	-
Reserves & Surplus	7,725	9,380	11,578	14,295
<b>Shareholders' Funds</b>	<b>7,829</b>	<b>9,483</b>	<b>11,682</b>	<b>14,398</b>
Minority Interest	193	847	947	1,047
Total Loans	171	426	346	296
<b>Total Liabilities</b>	<b>8,193</b>	<b>10,756</b>	<b>12,974</b>	<b>15,741</b>
<b>APPLICATION OF FUNDS</b>				
Gross Block	2,334	4,552	5,002	5,352
Less: Acc. Depreciation	801	2,029	2,304	2,598
<b>Net Block</b>	<b>1,533</b>	<b>2,253</b>	<b>2,698</b>	<b>2,754</b>
Capital Work-in-Progress	145	271	271	271
Goodwill on consolidation	406	772	772	772
<b>Investments</b>	<b>3,166</b>	<b>2,231</b>	<b>2,231</b>	<b>2,231</b>
Current Assets	3,612	6,017	8,071	10,964
Cash	509	2,194	2,880	4,784
Loans & Advances	849	1,128	1,604	1,948
Other	6	45	49	54
Current liabilities	758	1,423	1,333	1,416
<b>Net Current Assets</b>	<b>2,854</b>	<b>4,594</b>	<b>6,737</b>	<b>9,548</b>
Miscellaneous Expenditure	-	-	-	-
Net Deferred Tax	89	365	265	165
<b>Total Assets</b>	<b>8,193</b>	<b>10,756</b>	<b>12,974</b>	<b>15,741</b>

**Key Ratios**

Y/E March	FY2010	FY2011	FY2012E	FY2013E
<b>Valuation Ratio (x)</b>				
P/E (on FDEPS)	42.5	31.6	25.4	21.0
P/CEPS	38.2	28.4	22.7	19.0
P/BV	7.3	6.1	4.9	4.0
Dividend yield (%)	2.5	0.6	0.6	0.6
EV/Sales	13.9	9.6	7.1	5.9
EV/EBITDA	40.7	28.2	18.4	15.0
EV / Total Assets	6.9	5.6	4.6	3.6
<b>Per Share Data (Rs)</b>				
EPS (Basic)	13.0	17.5	21.8	26.4
EPS (fully diluted)	13.0	17.5	21.8	26.4
Cash EPS	14.5	19.5	24.5	29.2
DPS	13.8	3.5	3.5	3.5
Book Value	75.6	91.6	112.8	139.0
<b>Returns (%)</b>				
RoCE	17.7	20.5	24.3	23.4
RoIC	18.6	26.5	33.6	36.6
RoE	17.3	19.1	19.3	19.0
<b>Turnover ratios (x)</b>				
Asset Turnover (Gross Block)	1.7	1.3	1.5	1.7
Inventory / Sales (days)	96	81	79	81
Receivables (days)	96	75	69	78
Payables (days)	52	65	73	67
WCC (days)	209	153	184	196

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