

INDUSTRY PHARMA
CMP (as on 31 Oct 2017) Rs 827
Target Price Rs 1,200

Nifty 10,335

Sensex 33,213

KEY STOCK DATA

Bloomberg STR IN

No. of Shares (mn) 89

MCap (Rs bn) / (\$ mn) 74/1,143

6m avg traded value (Rs mn) 393

STOCK PERFORMANCE (%)
52 Week high / low Rs 1,275/802

3M 6M 12M

Absolute (%) (21.9) (22.9) (20.6)

Relative (%) (24.0) (33.9) (39.5)

SHAREHOLDING PATTERN (%)

Promoters 31.1

FIs & Local MFs 15.9

FPIs 34.2

Public & Others 18.8

Source : BSE

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Extended pit stop

Strides Shasun's (STR) 2QFY18 performance was an improvement over 1QFY18. However, the YoY performance remained subdued. Total revenues grew ~14% YoY to ~Rs 10bn. Sequential growth was higher at ~18%. This was driven by a ~21% QoQ jump in regulatory market sales. EBITDA came in at ~Rs 1.3bn (-15% YoY), and the margin was 13.2%, down ~450bps YoY. Although there was a sequential improvement, it was lower than expectations. PAT came in at Rs 215mn, down ~75% YoY, leaving a long way to go to achieve our FY18 estimate of ~Rs 3.1bn.

Margin performance during this quarter was a confluence of several negative factors like (1) inferior business mix (higher contribution from APIs), (2) Adverse product mix in the institutional business, and (3) Higher marketing spends on the Consumer Healthcare business in the US and India (Rs 161mn). We believe that this is likely to reverse in 2HFY18, on the back of higher sales in the US (driven by key product launches in Sep-17), absence of APIs from the business mix (hive-off), supplies of anti-malarial tenders in the institutional business and lower

Financial Summary

(Rs mn)	2QFY18	2QFY17	YoY (%)	1QFY17	QoQ (%)	FY17	FY18E	FY19E	FY20E
Net Sales	9,956	8,720	14.2	8,418	18.3	34,131	37,119	40,149	47,106
EBITDA	1,312	1,540	(14.8)	873	50.2	6,428	6,162	7,709	9,657
APAT	215	863	(75.2)	33	556.0	3,045	3,121	4,611	6,050
Diluted adj. EPS (Rs/sh)	2.4	9.6	(75.2)	0.4	556.0	34.0	34.9	51.5	67.6
EV/EBITDA (x)						15.8	26.7	17.1	13.0
RoE (%)						13.1	11.6	16.0	18.3

Source: Company, HDFC sec Inst Research # Consolidated

marketing costs. The operating leverage from the US and Australia will likely result in a steep improvement in profitability in 2HFY18.

Overall, we continue to believe that STR possesses the potent combination of high growth potential, a strong regulatory record and comfortable valuations. Maintain BUY with a TP of Rs 1,200 (18x Sep19E + Rs 100/sh for Solara + Rs 30/sh for biopharma).

Highlights of the quarter

- Takeaways:** (1) The partnership with Par for gLovaza gives instant access to 25% of the market, economic terms are in STR's favour, (2) Potassium citrate launch is progressing well, full impact to be seen in 3QFY18, (3) Expect a quarterly run-rate of US\$45-50mn in the US by the end of FY18, (4) Early teens growth in Australia in value and volumes, much ahead of the market, (5) Backward integration in Aus has started, this process will help offset PBS price erosion and add 3-5% to Aus biz gross margin, and (6) Expect to retain market share in upcoming anti-malarial tender.
- Near-term outlook:** 2HFY18 will be strong, with the launches of gLovaza and potassium citrate in Sep-17.

Top-line performance was good, led by 13% YoY growth in the regulatory business

Other expenses were higher, largely on account of the marketing spends on the consumer healthcare businesses in the US and India

Gross margin was lower owing to (1) Inferior business mix (higher contribution from APIs), and (2) Adverse product mix in the institutional business

Quarterly Financials Snapshot (Consolidated)

Particulars	2QFY18	2QFY17	YoY (%)	1QFY17	QoQ (%)
Net Sales	9,956	8,720	14.2	8,418	18.3
Material Expenses	4,837	3,739	29.4	4,193	15.4
Employee Expenses	1,577	1,556	1.4	1,465	7.7
Other Expenses	2,230	1,885	18.3	1,887	18.2
EBITDA	1,312	1,540	(14.8)	873	50.2
Depreciation	543	444		511	
EBIT	769	1,096	(29.8)	362	112.6
Other Income	223	546		361	
Interest Cost	619	580		640	
PBT	373	1,062	(64.9)	82	354.0
Exceptional items	(139)	(122)		(27)	
Tax	42	129		(33)	
Profit / (Loss) from Discontinued Operations	(32)	45		-	
Minority Interest & Profit/(Loss) of Associate Company	(84)	(114)		(83)	
RPAT	76	741	(89.8)	6	1,255.4
EO Items (Adj For Tax)	(139)	(122)		(27)	
APAT	215	863	(75.2)	33	556.0

Source: Company, HDFC sec Inst Research

Margin Analysis

	2QFY18	2QFY17	YoY (bps)	1QFY17	QoQ (bps)
Material Expenses % Net Sales	48.6	42.9	570	49.8	(123)
Employee Expenses % Net Sales	15.8	17.8	(200)	17.4	(156)
Other Expenses % Net Sales	22.4	21.6	78	22.4	(2)
EBITDA Margin (%)	13.2	17.7	(448)	10.4	280
Tax Rate (%)	13.2	17.7	(448)	10.4	280
APAT Margin (%)	11.2	12.2	(100)	(40.7)	5,184

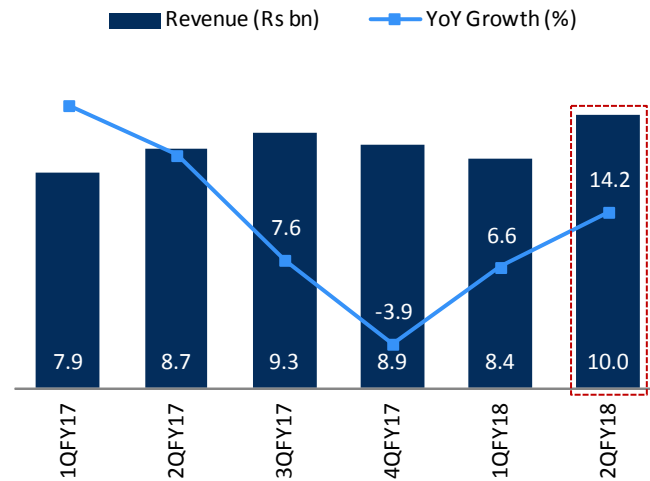
Source: Company, HDFC sec Inst Research

We believe that 2HFY18 will see a much stronger revenue performance on the back of key product launches in the US market in Sep-17

Anti-malarial tender should boost growth in the emerging markets segment. African branded business is showing mid-teens growth and productivity is improving

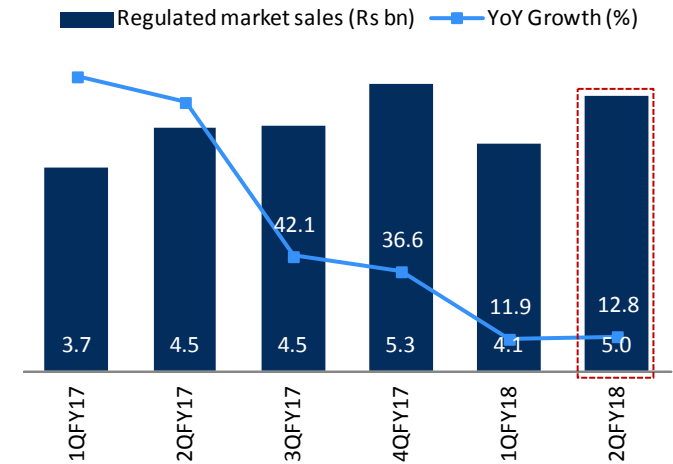
EBITDA margin to have a strong recovery in 2HFY18, primarily driven by operating leverage

Revenue: Strong Sequential Growth



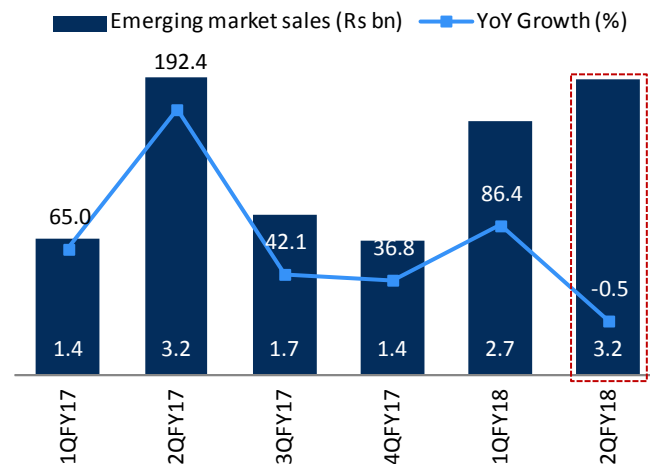
Source: Company, HDFC sec Inst Research

Regulated Markets: US Launches To Drive Growth



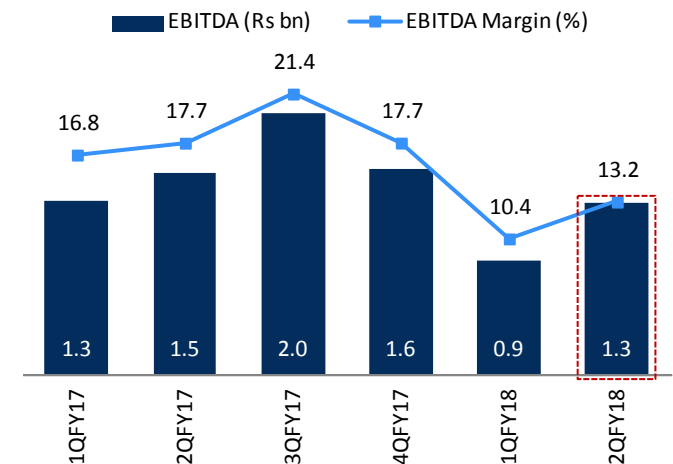
Source: Company, HDFC sec Inst Research

Emerging Markets: Adverse Product Mix Impacts Growth



Source: Company, HDFC sec Inst Research

EBITDA Margin: 2HFY18 To See Strong Recovery



Source: Company, HDFC sec Inst Research

Segmental Quarterly Performance

(Rs mn)	2QFY18	2QFY17	YoY (%)	1QFY17	QoQ (%)
Regulated markets	5,025	4,453	12.8	4,147	21.2
Emerging markets	3,152	3,167	(0.5)	2,697	16.9
API	1,830	835	119.2	1,514	20.9
Total	10,007	8,455	18.4	8,358	19.7

Source: HDFC sec Inst Research

Assumptions

	FY17	FY18E	FY19E	FY20E
Regulated markets	17,762	19,494	25,794	31,281
<i>Growth (%)</i>	55.9	9.8	32.3	21.3
Emerging markets	12,007	12,797	14,094	15,528
<i>Growth (%)</i>	22.6	6.6	10.1	10.2
API	5,336	3,068	-	-
<i>Growth (%)</i>	(27.0)	(42.5)	(100.0)	N/A
Total	35,105	35,360	39,888	46,810
<i>Growth (%)</i>	23.2	0.7	12.8	17.4

Source: HDFC sec Inst Research

Peer Valuations

	Mcap (Rs bn)	CMP (Rs/sh)	Reco	TP	Adj EPS (Rs/sh)				P/E (x)				RoE (%)			
					FY17	FY18E	FY19E	FY20E	FY17	FY18E	FY19E	FY20E	FY17	FY18E	FY19E	FY20E
Sun Pharma	1,330	553	NEU	525	26.0	15.8	23.0	30.8	21.3	35.0	24.1	17.9	17.9	10.1	13.6	16.1
Cadila Healthcare	516	503	BUY	570	14.5	14.4	19.1	26.5	34.6	35.0	26.3	19.0	23.5	19.0	20.8	23.6
Cipla	504	628	NEU	565	12.5	18.4	24.7	31.7	50.2	34.2	25.4	19.8	8.4	11.2	13.5	15.2
Lupin	462	1,028	BUY	1,565	56.9	41.2	61.5	80.6	18.1	25.0	16.7	12.8	20.9	13.1	17.4	19.4
Aurobindo Pharma	445	760	BUY	820	39.3	40.1	48.0	54.2	19.3	18.9	15.8	14.0	27.6	22.5	21.8	20.2
Dr Reddy's Labs	412	2,428	SELL	2,220	72.7	71.0	118.8	158.9	33.4	34.2	20.4	15.3	9.5	9.2	14.1	16.6
Divi's Labs	234	883	NEU	795	39.9	33.0	40.9	46.7	22.1	26.8	21.6	18.9	22.0	15.5	17.4	17.9
Alkem Laboratories	224	1,874	BUY	2,060	74.6	64.9	87.9	108.2	25.1	28.9	21.3	17.3	21.9	16.3	19.2	20.3
Torrent Pharma	215	1,270	BUY	1,400	51.2	46.9	60.7	79.0	24.8	27.1	20.9	16.1	22.1	17.8	20.6	22.7
Glenmark	174	618	BUY	1,035	29.6	27.2	43.7	55.1	20.9	22.7	14.1	11.2	18.1	14.1	19.0	19.9
Jubilant Life Sciences	102	640	BUY	850	37.0	42.1	55.2	70.9	5.3	4.6	3.5	2.7	18.0	17.9	19.8	21.1
Alembic Pharma	95	505	BUY	650	21.4	21.0	27.7	37.2	23.6	24.1	18.2	13.6	23.0	19.4	21.8	24.2
Strides Shasun	74	829	BUY	1,200	34.0	34.9	51.5	67.6	24.4	23.8	16.1	12.3	13.1	11.6	16.0	18.3
Dishman Carbogen Amcis	48	297	BUY	405	9.0	12.3	16.7	23.8	33.0	24.2	17.8	12.5	3.0	4.0	5.3	7.1
Granules India	32	140	BUY	190	7.2	8.4	10.6	13.3	19.4	16.5	13.2	10.5	21.0	19.6	20.7	22.2

Source: HDFC sec Inst Research

Change In Estimates (Consolidated)

Rs mn	Previous			New			% Chg		
	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E
Net Sales	35,360	39,888	46,810	37,119	40,149	47,106	5.0	0.7	0.6
EBITDA	6,471	7,658	9,596	6,162	7,709	9,657	(4.8)	0.7	0.6
APAT	3,578	4,592	6,040	3,121	4,611	6,050	(12.8)	0.4	0.2

Source: HDFC sec Inst Research

Income Statement (Consolidated)

Year ending March (Rs mn)	FY16	FY17	FY18E	FY19E	FY20E
Net Revenues	28,044	34,131	37,119	40,149	47,106
Growth (%)	134.5	21.7	8.8	8.2	17.3
Material Expenses	15,023	15,362	17,260	17,866	20,491
Employee Expenses	3,577	5,881	5,716	6,424	7,066
Other Operating Expenses	5,304	6,459	7,981	8,150	9,892
EBITDA	4,140	6,428	6,162	7,709	9,657
EBITDA Margin (%)	14.8	18.8	16.6	19.2	20.5
EBITDA Growth (%)	80.9	55.3	(4.1)	25.1	25.3
Depreciation	1,313	1,872	1,887	1,801	1,977
EBIT	2,827	4,556	4,275	5,907	7,680
Other Income (Including EO Items)	921	1,686	1,750	1,850	1,950
Interest	1,682	2,269	1,965	1,696	1,581
Exceptional Items	(414)	(1,006)	(166)	-	-
PBT	1,653	2,967	3,894	6,061	8,049
Tax (Incl Deferred)	425	470	589	1,000	1,449
Profit/(loss) from discontinuing operations	(232)	1,959	-	-	-
Profit/(loss) of associate company	(47)	4	-	-	-
Minority Interest	135	(462)	(350)	(450)	(550)
RPAT	1,085	3,997	2,955	4,611	6,050
EO (Loss) / Profit (Net Of Tax)	(645)	953	166	-	-
APAT	1,730	3,045	3,121	4,611	6,050
APAT Growth (%)	1836.0	75.9	2.5	47.7	31.2
Adjusted EPS (Rs)	20.8	34.0	34.9	51.5	67.6

Source: Company, HDFC sec Inst Research

Balance Sheet (Consolidated)

Year ending March (Rs mn)	FY16	FY17	FY18E	FY19E	FY20E
SOURCES OF FUNDS					
Share Capital - Equity	893	894	894	894	894
Reserves	25,685	26,210	28,811	32,730	37,691
Total Shareholders Funds	26,579	27,104	29,705	33,624	38,586
Minority Interest	502	1,640	1,990	2,440	2,990
Long Term Debt	26,270	16,377	11,877	10,877	9,877
Short Term Debt	7,005	13,940	13,940	13,940	13,940
Total Debt	33,275	30,317	25,817	24,817	23,817
Net Deferred Taxes	(502)	88	230	150	100
Other Non-current Liabilities & Provns	1,833	4,855	5,120	5,500	5,650
TOTAL SOURCES OF FUNDS	61,686	64,004	62,862	66,531	71,142
APPLICATION OF FUNDS					
Net Block	17,520	19,462	15,485	18,184	20,206
CWIP	8,149	7,802	7,500	5,250	3,150
Goodwill	9,267	9,670	9,670	9,670	9,670
Investments	1,272	3,157	3,906	4,226	4,578
Other Non-current Assets	2,245	2,212	2,900	3,100	3,400
Total Non-current Assets	38,452	42,302	39,460	40,429	41,004
Cash & Equivalents	15,253	16,090	11,758	15,225	16,964
Inventories	6,131	7,380	7,119	8,250	9,679
Debtors	10,330	9,971	11,186	11,000	12,906
Other Current Assets	3,434	4,734	5,364	5,554	6,286
Total Current Assets	19,896	22,084	23,669	24,803	28,871
Creditors	7,754	7,465	7,093	8,811	9,824
Other Current Liabilities & Provns	4,161	9,006	4,932	5,115	5,872
Total Current Liabilities	11,915	16,471	12,025	13,926	15,696
Net Current Assets	7,981	5,613	11,643	10,878	13,175
TOTAL APPLICATION OF FUNDS	61,686	64,005	62,862	66,531	71,143

Source: Company, HDFC sec Inst Research

Cash Flow

Year ending March (Rs mn)	FY16	FY17	FY18E	FY19E	FY20E
Reported PBT	1,464	4,971	4,060	6,061	8,049
Non-operating & EO items	941	(1,599)	142	(80)	(50)
Interest net	995	1,521	1,965	1,696	1,581
Depreciation	1,520	1,987	1,887	1,801	1,977
Working Capital Change	(3,417)	(3,413)	(6,454)	946	(2,447)
Tax Paid	(770)	(586)	(589)	(1,000)	(1,449)
OPERATING CASH FLOW (a)	732	2,881	1,011	9,424	7,661
Capex	(3,691)	(6,823)	2,302	(2,250)	(1,900)
Free cash flow (FCF)	(2,959)	(3,942)	3,313	7,174	5,761
Investments	(18,506)	(647)	530	(896)	(957)
Non-operating Income	471	846	-	-	-
Others	(521)	(427)	-	-	-
INVESTING CASH FLOW (b)	(22,248)	(7,051)	2,832	(3,146)	(2,857)
Debt Issuance/(Repaid)	19,115	6,037	(4,500)	(1,000)	(1,000)
Interest Expenses	(1,347)	(2,370)	(1,965)	(1,696)	(1,581)
FCFE	(3,748)	(502)	(2,622)	3,582	2,224
Share Capital Issuance	12,264	165	(0)	0	(0)
Dividend	(265)	(451)	(355)	(692)	(1,089)
Others	(327)	-	(76)	-	-
FINANCING CASH FLOW (c)	29,439	3,382	(6,895)	(3,388)	(3,670)
NET CASH FLOW (a+b+c)	7,924	(788)	(3,052)	2,891	1,134
EO Items, Others	195	(5,169)	-	-	-
Closing Cash & Equivalents	11,107	5,151	243	3,133	4,268

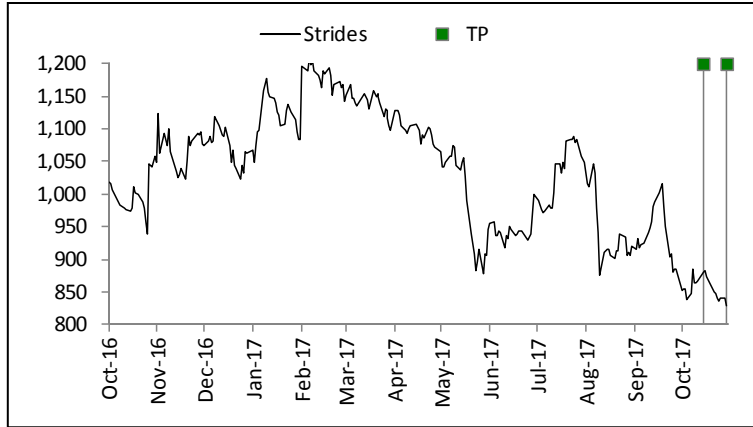
Source: Company, HDFC sec Inst Research

Key Ratios

	FY16	FY17	FY18E	FY19E	FY20E
PROFITABILITY (%)					
GPM	46.4	55.0	53.5	55.5	56.5
EBITDA Margin	14.8	18.8	16.6	19.2	20.5
APAT Margin	5.7	10.3	8.9	12.6	14.0
RoE	8.4	13.1	11.6	16.0	18.3
RoIC (or Core RoCE)	10.8	12.0	11.0	13.6	16.2
RoCE	1.2	4.8	8.5	7.6	9.3
EFFICIENCY					
Tax Rate (%)	20.5	11.8	14.5	16.5	18.0
Fixed Asset Turnover (x)	1.5	1.5	1.8	1.6	1.6
Inventory (days)	79.8	78.9	70.0	75.0	75.0
Debtors (days)	134.4	106.6	110.0	100.0	100.0
Other Current Assets (days)	40.7	36.4	41.8	41.4	40.7
Payables (days)	100.9	79.8	69.8	80.1	76.1
Other Current Liab & Provns (days)	52.2	94.3	46.5	44.5	43.5
Cash Conversion Cycle (days)	101.8	47.8	105.5	91.8	96.1
Debt/EBITDA (x)	8.0	4.7	4.2	3.2	2.5
Net D/E (x)	1.1	1.0	0.9	0.6	0.2
Interest Coverage (x)	2.2	2.8	3.1	4.6	6.1
PER SHARE DATA (Rs)					
EPS	18.0	55.9	33.0	51.5	67.6
Dividend	4.0	4.5	3.3	6.4	10.1
Book Value	297.1	302.9	332.0	375.8	431.3
VALUATION					
P/E (x)	46.0	14.8	25.1	16.1	12.3
P/BV (x)	2.8	2.7	2.5	2.2	1.9
EV/EBITDA (x)	25.2	15.7	16.2	12.4	9.7
EV/Revenues (x)	3.7	3.0	2.7	2.4	2.0
OCF/EV (%)	0.7	2.8	1.0	9.8	8.2
FCF/EV (%)	(2.8)	(3.9)	3.3	7.5	6.1
FCFE/Mkt Cap (%)	(5.1)	(0.7)	(3.5)	4.8	3.0
Dividend Yield (%)	0.5	0.5	0.4	0.8	1.2

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
16-Oct-17	881	BUY	1,200
1-Nov-17	827	BUY	1,200

Rating Definitions

- BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
- NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
- SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

INSTITUTIONAL RESEARCH

Disclosure:

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