

Sun Pharmaceutical Industries Ltd. (Sun Pharma) enjoys the status of being the fifth largest pharma company in the world and the largest generic drug maker in India. With the market cap of more than ₹2 trillion, the company has presence spanning across 150 countries across branded and generic markets. The broader segment of the company includes Specialty products, branded generics, complex generics, pure generics & APIs. Its portfolio comprises of more than 3,000 products. The company has a strong R&D base with capabilities across dosage forms like injectables, sprays, ointments, creams, liquids, tablets and capsules. Sun Pharma is the 5th largest generics company in the US market, while enjoying the dominance in higher growth chronic therapies in Indian branded generics market.

Investment Rationale

Strong product pipeline augurs well for Sun Pharma

Sun Pharma is having a strong product pipeline in the US market, with 159 products fillings awaiting USFDA approval. Overall, the company has filled for 1,598 patents, while revived patents approval of 951 till FY15.

Astra Zeneca deal to consolidate the company's cardio portfolio

Sun Pharma recently inked a pact for promoting and distributing "Axcer" brand in India. This is the brand of AstraZeneca Pharma which is looking to expand usage of this molecule through wider reach to physicians and thereby benefiting a greater number of ACS patients. For Sun Pharma, the drug will strengthen its cardiology portfolio with the addition of a new patented therapy.

Revenue is expected to grow at a CAGR of ~30% YoY over FY14-17E

Despite posting disappointing numbers in Q4FY15, the company was able to report a hike of 71% in its annual sales. The reported decline in Q4FY15 profits was due to product erosions and integration costs translating into the books of accounts after the Ranbaxy acquisition. However, the management is of the view that the integration costs will be subsided after Q1FY16 and the company will be able to leverage on its positions in the Western Europe and other emerging markets that it attained post the merger. Hence, we believe that the company will be able to derive huge profits as a synergy arising for the Ranbaxy deal.

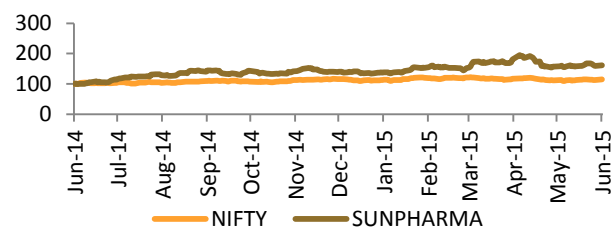
Market Data

Rating	BUY
CMP (₹)	867
Target (₹)	1,010
Potential Upside	~17%
Duration	Long Term
Face Value (₹)	1.0
52 week H/L (₹)	1,200.8/625
Adj. all time High (₹)	1,200.8
Decline from 52WH (%)	27.8
Rise from 52WL (%)	38.7
Beta	1.0
Mkt. Cap (₹cr)	2,08,600.2
EV (₹cr)	2,05,198.5

Fiscal Year Ended

Y/E	FY14A	FY15A	FY16E	FY17E
Revenue (₹cr)	16,080.4	27,433.4	42,796.2	66,762.0
EBITDA (₹cr)	7,190.1	8,063.6	13,661.7	21,216.7
Net Profit (₹cr)	3,141.5	4,540.1	9,525.8	15,427.7
EPS (₹)	27.3	23.1	46.0	74.5
P/E (x)	29.6	34.4	17.5	11.2
P/BV (x)	8.8	7.9	5.0	3.5
EV/EBITDA (x)	28.3	25.8	15.1	9.8
ROCE (%)	30.6	21.5	31.2	36.4
ROE (%)	27.7	18.0	26.7	30.4

One year relative price chart



Shareholding Pattern	10 Apr 15	Mar 15	Diff.
Promoters	54.7	63.6	(8.9)
FII	18.8	20.0	(1.2)
DII	5.2	4.6	0.6
Others	21.3	11.9	9.4

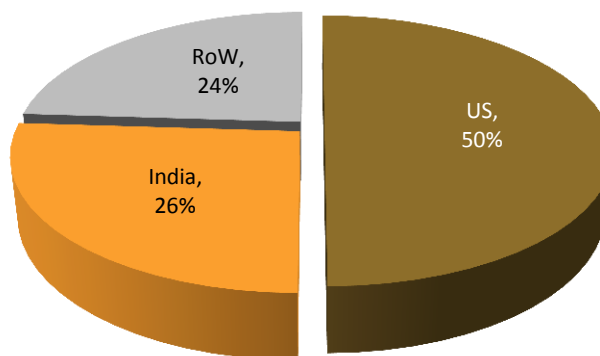
Sun Pharma is the 5th largest global specialty generic company, with a diverse market presence in more than 150 countries across branded and generic markets.

With the company having a large market share, strong R&D capabilities and highly diversified revenue stream, we believe Sun Pharma can translate its growth trajectory going ahead and also bank on future expansion projects.

Sun Pharma – the 5th largest pharma company in the world

Sun Pharmaceutical Industries Ltd. (Sun Pharma) enjoys the status of being the 5th largest pharma company in the world and the largest generic drug maker in India. With the market cap of more than ₹2 trillion, Sun Pharma has presence spanning across 150 countries across branded and generic markets. The broader segment of the company includes specialty products, branded generics, complex generics, pure generics & APIs. Its portfolio comprises of more than 3,000 products. The company has strong R&D base with capabilities across dosage forms like injectables, sprays, ointments, creams, liquids, tablets and capsules. Sun Pharma is the 5th largest generics company in the US market, while enjoying dominance in higher growth chronic therapies in Indian branded generics market. Sun Pharma has evolved into an international, integrated, specialty pharmaceutical company with 45 manufacturing facilities spread across 5 continents, R&D centres across the globe. Sun Pharma led its inorganic growth through various acquisitions and joint ventures all over the world.

Revenue segmentation - Geographical



Strong play-up on the expansion front

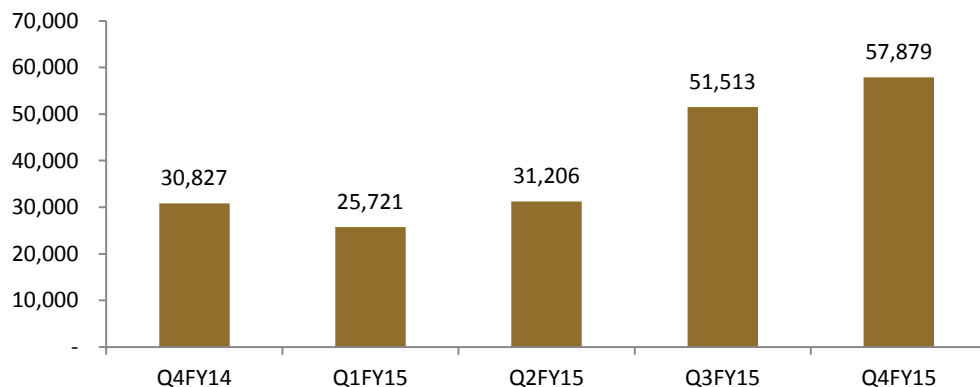
Ever since its inception, Sun Pharma has used acquisitions to bridge critical capability gaps and creating sustainable revenue streams. In its recent acquisition, Sun Pharma acquired Ranbaxy from Daiichi Sankyo during Q4FY15 in an all-stock deal at \$3.2 billion including \$800 million of debt that was on the Ranbaxy books. The deal has given India's biggest drug maker sufficient scale in generics and emerging markets and the stature of the world's fifth largest drug-maker with ~9.1% market share in the world's drug market. Going forward, Sun Pharma intends to focus on boosting productivity as it looks to realise synergies to the tune of \$250 million over three years. As a part of the value creation chain, the company hopes to use this ambitious acquisition as a growth engine for future takeovers as it is thinking of beefing up expertise in higher margin products and gaining a bigger global presence. The company has earmarked a value of ~\$7 billion for further acquisitions fulfilling aforementioned objectives.

With the company having a large market share, strong R&D capabilities and highly diversified revenue stream, we believe Sun Pharma can translate its growth trajectory going ahead and also bank on future expansion projects.

Distribution deal with AstraZeneca will strengthen Sun Pharma's cardiology portfolio (the second largest product in India contributing to 16% of the Indian revenue) with the addition of a new patented therapy.

Sun Pharma is having one of the largest ANDAs pipeline (159 ANDAs awaiting approval).

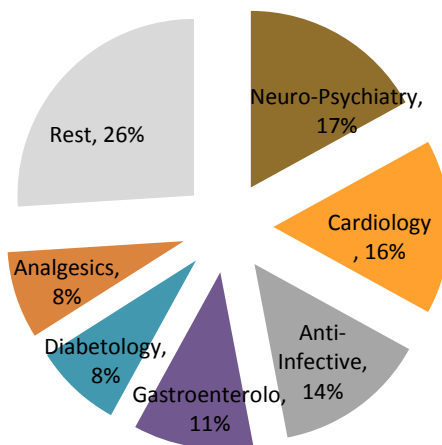
Growth in R&D expenses in last five quarters (₹ crore)



Distribution deal with AstraZeneca to strengthen Sun Pharma's cardiology portfolio

Sun Pharma has entered into a distribution services agreement to distribute AstraZeneca's heart disease treatment drug 'Axcer' in India. Axcer is a drug used for the treatment of acute coronary syndrome (ACS). As per the management, "Such collaborations are also part of the company's stated policy of becoming the partner of choice for promotion and distribution of innovative pharmaceutical products in the country." This collaboration will enable AstraZeneca to expand usage of this molecule through wider reach to physicians and thereby, benefiting a greater number of ACS patients. It will strengthen Sun Pharma's cardiology portfolio (the second largest product in India contributing to 16% of the Indian revenue) with the addition of a new patented therapy.

Therapeutic Portfolio in India as in Q4FY15

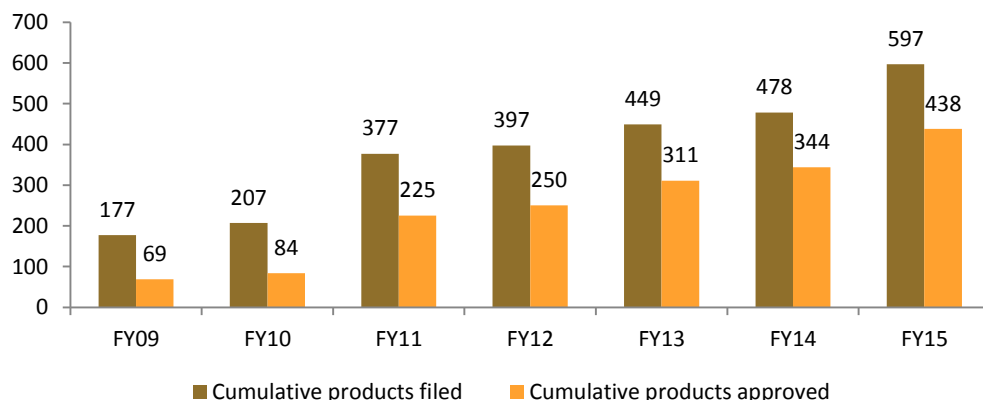


Strong product pipeline augurs well for Sun Pharma

Sun Pharma is the 5th largest generic company in the US market and is having a strong product pipeline in the US market with approved ANDAs for 438 products while 159 products fillings awaiting USFDA approval, including 12 tentative approvals at the end of FY15. Sun Pharma continues to incur R&D expenditure with a view to build strong product portfolio to earn higher return. For full year FY15, R&D spend of the company was ₹1,955 crore (7.2% of sales). Overall, the company has filled for 1,598 patents, while revived patents approval of 951 till FY15. This signifies the company commitment towards new product development in order to stay competitive in the pharmaceutical market globally.

Despite a disappointing (Q4FY15) quarter post the acquisition, the company was able to turnaround the earnings for FY15, with the revenue increasing by ~71%, while the bottom-line rose 44.5%.

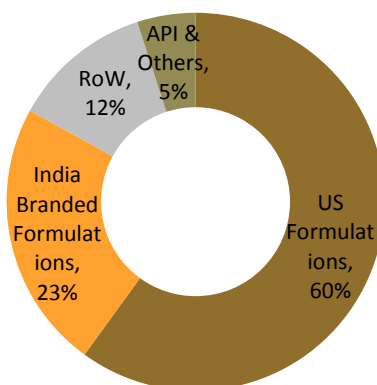
Significant ramp-up in ANDA pipeline



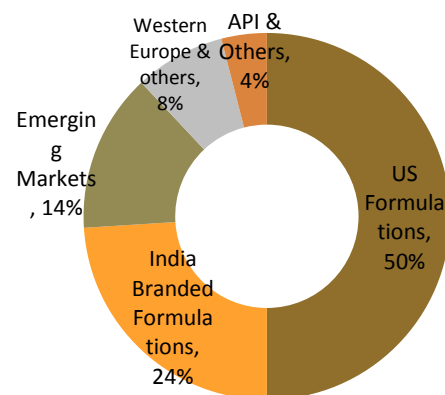
FY15 performance

After an eventful FY15, Sun Pharma reported its first yearly numbers post Ranbaxy acquisition and witnessed a massive rise in the top-line. The revenue increased by ~71%, while the bottom-line rose 44.5%. Despite a disappointing (Q4FY15) quarter post the acquisition, the company was able to turnaround the earnings for the entire year. Sun Pharma retained its leadership position in India's branded generics space. Sale of branded prescription formulations in India for FY15 stood at ₹6,717 crore. US formulations sales in the US were at \$2,244 million for FY15, accounting for 50% of the total sales. A bulk of these sales came from Taro which recently posted full year sales of \$863 million, up by 14% over the last fiscal. Further, sales from emerging market for FY15 (accounting for 14% of the total sales) was at \$611 million. On the margins front, the company witnessed ~1,530 bps decline due to higher costs. The EBITDA margin declined from 44.7% in FY14 to 29.4% in FY15. As a result, the PAT margin declined to 17% from 20% over FY14.

Pre-acquisition revenue-base



Post-acquisition revenue-base



Struggled on margins front despite robust revenue growth in Q4FY15

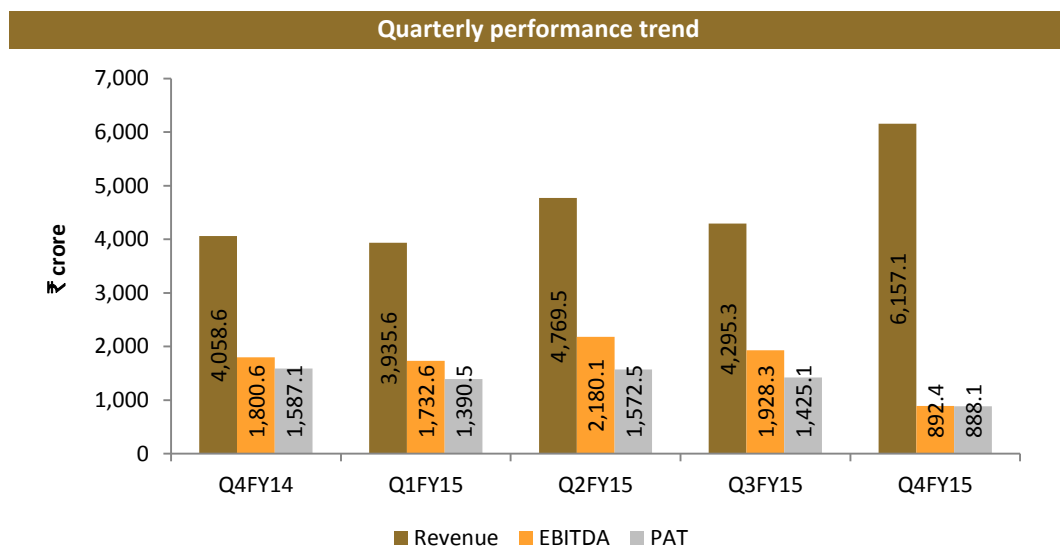
Sun Pharmaceutical Industries Ltd reported consolidated net sales of ₹6,157.1 crore in Q4FY15, up 51.7% from ₹4,058.3 crore for the same period of the last fiscal. The operating expenses of the company stood at ₹5,264.7 crore, higher by 133.15% YoY against ₹2,258 crore in Q4FY14. Because of the significant increase in the operating expenses, the EBITDA fell by 50.44% YoY to ₹892.4 crore from ₹1,800.6 crore in the same session for last year.

While the consolidated total income surged 51.7% YoY, the EBITDA and bottom-line was adversely affected by the Ranbaxy merger.

We believe that the approval received by the company to start manufacturing at its Halol facility will aid sales in the near term and will be able to sustain its past growth.

As a result, the operating profit margins were reported at 14.5% as against 44.4% in the year ago period. The performance of the company was hugely impacted due to various one time charges paid in the Ranbaxy merger deal.

Depreciation and other expenses dragged the bottom line - As against 51.7% increase in the net sales, the company reported a significant decrease in its bottom line, which fell by 44.05% YoY and stood at ₹888.1 crore in Q4FY15 as against ₹1,587.1 crore in Q4FY14. The downfall in net profit was mainly due to merger impact with Ranbaxy and the price crunching of some products of the company in the US markets. Further, sharp rise in depreciation and amortization numbers by 429.6% to ₹561.9 crore from ₹106.10 crore in the corresponding quarter of last year, also dragged the profit.



Resumption of manufacturing at Halol: a key factor

With the acquisition of Ranbaxy, Sun Pharma's quarterly numbers suffered the complexity of integration with the process taking longer time than earlier estimated by the management. The management is aiming at cultural integration: ensuring compliance of good manufacturing practices, targeting more product filings, improving productivity and achieving revenue integration and efficient procurement. Sun Pharma will also have to work on reviving Ranbaxy's domestic and US growth. Ranbaxy is seeing declining US sales and its India business too is facing challenges. The US remains the largest geography for Sun Pharma, contributing about 50% to its revenues in FY15. However, Sun Pharma's US subsidiary Taro alone posted \$244 million in sales as Sun Pharma's sales were lower than expectations. Meanwhile, the supplies to the US are constricted and there is price erosion in some products that is impacting prospects. However, we believe that the approval received by the company to start manufacturing at its Halol facility will aid sales in the near term and will be able to sustain its past growth.

Key risks

- Adverse currency movements
- Increased competition in US derma market
- Delay in product approval
- Potential future adverse inspections from USFDA

Balance Sheet (Consolidated)

Y/E (₹cr)	FY14A	FY15A	FY16E	FY17E
Share Capital	207.1	255.4	207.1	207.1
Reserves & Surplus	18,317.8	26,251.5	34,183.1	48,191.8
Net worth	18,525.0	26,506.9	34,390.2	48,398.9
Minority interest	1,921.2	2,851.2	2,851.2	2,851.2
Long term borrowings	48.7	1,368.4	1,368.4	1,368.4
Other Long term Liabilities	9.1	186.3	186.3	186.3
Deferred tax liability(net)	275.7	98.5	98.5	98.5
Long term provisions	2,601.6	2,532.3	2,785.6	2,785.6
Short term provisions	1,960.6	3,336.4	3,403.1	3,471.1
Other current liabilities	4,029.0	12,147.7	11,973.5	12,340.1
Total equity & liabilities	29,370.8	49,027.8	57,056.9	71,500.2
Fixed assets	7,658.8	14,721.1	30,421.3	44,412.2
Investments	787.6	598.9	598.9	598.9
Loans & advances	1,051.2	2,680.5	2,708.3	2,736.4
Other non-current assets	1,186.8	1,905.5	55.4	55.4
Other current assets	18,686.5	29,121.8	23,273.1	23,697.4
Total assets	29,370.8	49,027.8	57,056.9	71,500.2

Profit & Loss Account (Consolidated)

Y/E (₹cr)	FY14A	FY15A	FY16E	FY17E
Total income	16,080.4	27,433.4	42,796.2	66,762.0
Operating Expenses	8,890.3	19,369.8	29,134.4	45,545.4
EBITDA	7,190.1	8,063.6	13,661.7	21,216.7
Other Income	362.4	452.1	492.7	537.1
Depreciation	409.2	1,294.8	748.2	643.0
EBIT	7,143.3	7,220.9	13,406.3	21,110.8
Interest	44.2	579.0	1,035.1	1,074.9
Exceptional items	2,517.4	237.8	0.0	0.0
PBT	7,099.1	6,641.9	12,371.2	20,035.9
Tax	702.7	914.6	2,845.4	4,608.3
PAT	3,879.0	5,489.5	9,525.8	15,427.7
Minority interest	737.5	956.3	0.0	0.0
Share in loss of asso. Co.	0.0	6.8	0.0	0.0
Reported Net Profit	3,141.5	4,540.1	9,525.8	15,427.7

Key Ratios (Consolidated)

Y/E	FY14A	FY15A	FY16E	FY17E
EBITDA Margin (%)	44.7	29.4	31.9	31.8
EBIT Margin (%)	44.4	26.3	31.3	31.6
NPM (%)	35.2	17.4	22.3	23.1
ROE (%)	27.7	18.0	26.7	30.4
EPS (₹)	27.3	23.1	46.0	74.5
P/E (x)	29.6	34.4	17.5	11.2
BVPS(₹)	98.7	110.2	172.2	245.1
P/BVPS (x)	8.8	7.9	5.0	3.5
EV/Net Sales (x)	12.7	7.5	4.8	3.1
EV/EBITDA (x)	28.3	25.8	15.1	9.8

Valuation and view

Ranbaxy acquisition marked the biggest takeover for Sun Pharma. In the near-term integration issues will surround the company to some extent. However, consistent outperformance in the domestic market with market share gains and high profitability reflect management's execution capability (and product selection skills). Identification of value-accretive assets and integrating them successfully has been one of the cornerstones of the company's success. So we believe that the company will be able to turnaround its profitability in the future.

At a current market price (CMP) of ₹867, the stock trades at a P/E of 17.5x FY16E and 11.2x FY17E. We recommend 'BUY' with a target price of ₹1,010, which implies potential upside of ~17% to the CMP from long term perspective.

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