

May 14, 2018

Surajit Pal
surajitpal@plindia.com
+91-22-66322259

Rating	Reduce
Price	Rs472
Target Price	Rs447
Implied Upside	-5.3%
Sensex	35,536
Nifty	10,807

(Prices as on May 11, 2018)

Trading data

Market Cap. (Rs bn)	1,132.1
Shares o/s (m)	2,399.3
3M Avg. Daily value (Rs m)	3275.6

Major shareholders

Promoters	54.30%
Foreign	16.32%
Domestic Inst.	16.23%
Public & Other	13.10%

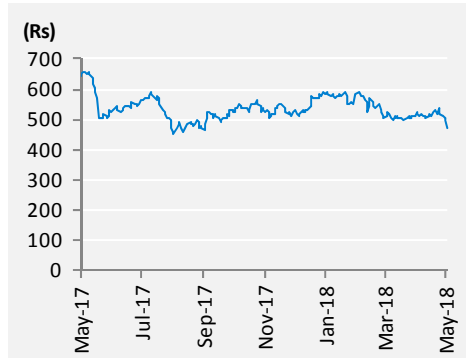
Stock Performance

(%)	1M	6M	12M
Absolute	(9.4)	(10.5)	(27.2)
Relative	(14.1)	(17.2)	(44.7)

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2019	16.1	13.6	18.9
2020	17.9	20.2	-11.5

Price Performance (RIC: SUN.BO, BB: SUNP IN)



Source: Bloomberg

Sun Pharma's partner Ciper, in their 1Q earnings conference call, highlighted sharp decline in their licensing revenue due to fall in Absorica (Isotretinoin) royalty. Absorica's licensing revenue decreased to US\$2.1m for Q1CY18, Vs US\$5.6m for Q1CY17.

The market share and prescriptions for Absorica decreased in Q1CY18. Absorica's (market size of US\$150-160m) market share, which peaked at 25% during 2017, ended at approximately 11-12% in Q1CY18, similar to the levels experienced prior to the promotional campaign.

Dr Reddy's Zenatane (a competitive drug to Absorica) exited the market in 2017. Sun Pharma's strategy to make a significant correction in its co-pay program, in order to increase profitability, could have caused them to lose market share in the drug. With Dr Reddy's exit, Sun Pharma could have gained market share in Isotretinoin, but management's belief that volumes wouldn't be impacted with reduction in co-pay program, led to decline in Sun's market share in the molecule.

Both, Akorn (from 25% to 41%) and Mylan (from 1-2% to 11%) with aggressive strategies, gained market share, while Dr. Reddy and Sun Pharma lost market share in Q1CY18. Sun Pharma reduced shipments to their distributors as inventory levels were adjusted to reflect the previously mentioned decrease in demand. Ciper expects Absorica sales to be muted for this quarter as well.

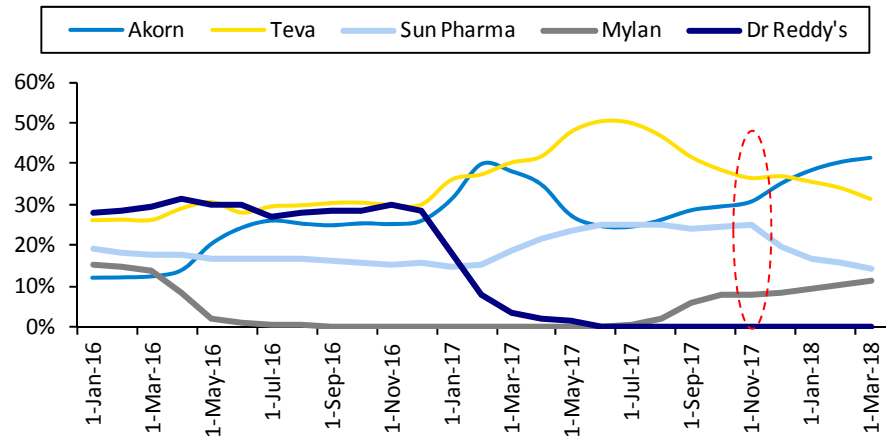
We believe Sun Pharma, being marketing partner for this product, would face the heat in Q4FY18 and going forward. The stock currently trades at 29x and 26x FY19E and FY20E respectively. We maintain our rating 'Reduce' with TP at Rs447.

Key financials (Y/e March)	2017	2018	2019E	2020E
Revenues (Rs m)	302,642	261,500	279,957	299,906
Growth (%)	8.5	(13.6)	7.1	7.1
EBITDA (Rs m)	87,751	52,562	60,191	65,979
PAT (Rs m)	69,644	28,293	38,677	42,890
EPS (Rs)	29.0	11.8	16.1	17.9
Growth (%)	33.5	(59.4)	36.7	10.9
Net DPS (Rs)	2.2	2.2	2.2	2.2

Profitability & Valuation	2017	2018	2019E	2020E
EBITDA margin (%)	29.0	20.1	21.5	22.0
RoE (%)	20.0	8.1	11.1	11.2
RoCE (%)	16.3	7.1	9.5	9.7
EV / sales (x)	3.6	4.2	3.8	3.4
EV / EBITDA (x)	12.3	20.7	17.6	15.5
PE (x)	16.3	40.0	29.3	26.4
P / BV (x)	3.1	3.4	3.1	2.8
Net dividend yield (%)	0.5	0.5	0.5	0.5

Source: Company Data; PL Research

Exhibit 1: TRx (weekly) share of brands in Isotretinoin for Absorica and peers



Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2017	2018	2019E	2020E
Net Revenue	302,642	261,500	279,957	299,906
Raw Material Expenses	81,307	73,743	78,388	79,475
Gross Profit	221,335	187,757	201,569	220,431
Employee Cost	49,023	54,131	55,991	58,482
Other Expenses	84,561	81,065	85,387	95,970
EBITDA	87,751	52,562	60,191	65,979
Depr. & Amortization	12,648	13,858	16,578	18,949
Net Interest	3,998	4,624	3,932	3,029
Other Income	19,374	8,912	9,357	9,825
Profit before Tax	90,479	42,992	49,038	53,826
Total Tax	12,116	11,149	6,865	7,536
Profit after Tax	78,363	31,843	42,172	46,291
Ex-Od items / Min. Int.	8,719	3,550	3,496	3,400
Adj. PAT	69,644	28,293	38,677	42,890
Avg. Shares O/S (m)	2,399.3	2,399.3	2,399.3	2,399.3
EPS (Rs.)	29.0	11.8	16.1	17.9

Cash Flow Abstract (Rs m)

Y/e March	2017	2018	2019E	2020E
C/F from Operations	85,132	(23,495)	23,350	35,146
C/F from Investing	(25,196)	(13,000)	(13,000)	(13,000)
C/F from Financing	(7,802)	(2,591)	4,573	2,564
Inc. / Dec. in Cash	52,134	(39,087)	14,924	24,710
Opening Cash	103,710	155,844	116,757	131,681
Closing Cash	155,844	116,757	131,681	156,391
FCFF	44,899	47,558	32,511	39,573
FCFE	58,249	22,060	17,947	27,922

Key Financial Metrics

Y/e March	2017	2018	2019E	2020E
Growth				
Revenue (%)	8.5	(13.6)	7.1	7.1
EBITDA (%)	16.1	(40.1)	14.5	9.6
PAT (%)	33.1	(59.4)	36.7	10.9
EPS (%)	33.5	(59.4)	36.7	10.9
Profitability				
EBITDA Margin (%)	29.0	20.1	21.5	22.0
PAT Margin (%)	23.0	10.8	13.8	14.3
RoCE (%)	16.3	7.1	9.5	9.7
RoE (%)	20.0	8.1	11.1	11.2
Balance Sheet				
Net Debt : Equity	(0.1)	(0.1)	(0.2)	(0.3)
Net Wrkng Cap. (days)	196	284	273	271
Valuation				
PER (x)	16.3	40.0	29.3	26.4
P / B (x)	3.1	3.4	3.1	2.8
EV / EBITDA (x)	12.3	20.7	17.6	15.5
EV / Sales (x)	3.6	4.2	3.8	3.4
Earnings Quality				
Eff. Tax Rate	13.4	25.9	14.0	14.0
Other Inc / PBT	21.4	20.7	19.1	18.3
Eff. Depr. Rate (%)	6.7	6.9	7.7	8.3
FCFE / PAT	83.6	78.0	46.4	65.1

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2017	2018	2019E	2020E
Shareholder's Funds	366,396	330,856	363,474	400,306
Total Debt	98,318	72,819	58,255	46,604
Other Liabilities	29,547	35,748	39,851	43,897
Total Liabilities	494,261	439,423	461,580	490,808
Net Fixed Assets	149,403	148,546	144,967	139,018
Goodwill	55,362	55,362	55,362	55,362
Investments	18,371	18,717	19,116	19,574
Net Current Assets	263,565	210,506	235,174	269,150
<i>Cash & Equivalents</i>	<i>151,408</i>	<i>116,757</i>	<i>131,681</i>	<i>156,391</i>
<i>Other Current Assets</i>	<i>175,819</i>	<i>169,491</i>	<i>177,040</i>	<i>185,028</i>
<i>Current Liabilities</i>	<i>63,663</i>	<i>75,742</i>	<i>73,547</i>	<i>72,269</i>
Other Assets	7,560	6,292	6,961	7,704
Total Assets	494,261	439,423	461,580	490,808

Quarterly Financials (Rs m)

Y/e March	Q4FY17	Q1FY18	Q2FY18	Q3FY18
Net Revenue	68,252	61,667	65,901	65,982
EBITDA	12,357	10,535	13,153	13,984
<i>% of revenue</i>	<i>18.1</i>	<i>17.1</i>	<i>20.0</i>	<i>21.2</i>
Depr. & Amortization	3,382	3,466	3,587	3,393
Net Interest	450	1,094	1,574	953
Other Income	5,363	1,941	3,151	1,842
Profit before Tax	13,888	7,916	11,144	11,479
Total Tax	443	1,618	1,114	7,487
Profit after Tax	12,237	(4,249)	9,121	3,654
Adj. PAT	12,237	(4,249)	9,121	3,654

Key Operating Metrics (Rs m)

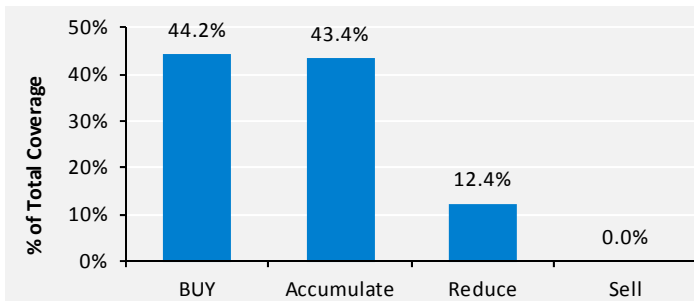
Y/e March	2017	2018	2019E	2020E
Formulations	280,207	246,400	263,221	281,957
India Formulations	78,341	80,691	90,374	100,315
US Formulations	135,301	97,836	98,234	99,634
ROW Formulations	66,565	67,873	74,613	82,008
APIs	16,068	17,165	19,045	20,509

Source: Company Data, PL Research.

**Prabhudas Lilladher Pvt. Ltd.**

3rd Floor, Sadhana House, 570, P. B. Marg, Worli, Mumbai-400 018, India

Tel: (91 22) 6632 2222 Fax: (91 22) 6632 2209

Rating Distribution of Research Coverage**PL's Recommendation Nomenclature**

BUY	:	Over 15% Outperformance to Sensex over 12-months
Accumulate	:	Outperformance to Sensex over 12-months
Reduce	:	Underperformance to Sensex over 12-months
Sell	:	Over 15% underperformance to Sensex over 12-months
Trading Buy	:	Over 10% absolute upside in 1-month
Trading Sell	:	Over 10% absolute decline in 1-month
Not Rated (NR)	:	No specific call on the stock
Under Review (UR)	:	Rating likely to change shortly

DISCLAIMER/DISCLOSURES**ANALYST CERTIFICATION**

We/I, Mr. Surajit Pal (PGDBA, CFA, M.Com), Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

Terms & conditions and other disclosures:

Prabhudas Lilladher Pvt. Ltd, Mumbai, India (hereinafter referred to as "PL") is engaged in the business of Stock Broking, Portfolio Manager, Depository Participant and distribution for third party financial products. PL is a subsidiary of Prabhudas Lilladher Advisory Services Pvt Ltd. which has its various subsidiaries engaged in business of commodity broking, investment banking, financial services (margin funding) and distribution of third party financial/other products, details in respect of which are available at www.plindia.com

This document has been prepared by the Research Division of PL and is meant for use by the recipient only as information and is not for circulation. This document is not to be reported or copied or made available to others without prior permission of PL. It should not be considered or taken as an offer to sell or a solicitation to buy or sell any security.

The information contained in this report has been obtained from sources that are considered to be reliable. However, PL has not independently verified the accuracy or completeness of the same. Neither PL nor any of its affiliates, its directors or its employees accepts any responsibility of whatsoever nature for the information, statements and opinion given, made available or expressed herein or for any omission therein.

Recipients of this report should be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The suitability or otherwise of any investments will depend upon the recipient's particular circumstances and, in case of doubt, advice should be sought from an independent expert/advisor.

Either PL or its affiliates or its directors or its employees or its representatives or its clients or their relatives may have position(s), make market, act as principal or engage in transactions of securities of companies referred to in this report and they may have used the research material prior to publication.

PL may from time to time solicit or perform investment banking or other services for any company mentioned in this document.

PL is in the process of applying for certificate of registration as Research Analyst under Securities and Exchange Board of India (Research Analysts) Regulations, 2014

PL submits that no material disciplinary action has been taken on us by any Regulatory Authority impacting Equity Research Analysis activities.

PL or its research analysts or its associates or his relatives do not have any financial interest in the subject company.

PL or its research analysts or its associates or his relatives do not have actual/beneficial ownership of one per cent or more securities of the subject company at the end of the month immediately preceding the date of publication of the research report.

PL or its research analysts or its associates or his relatives do not have any material conflict of interest at the time of publication of the research report.

PL or its associates might have received compensation from the subject company in the past twelve months.

PL or its associates might have managed or co-managed public offering of securities for the subject company in the past twelve months or mandated by the subject company for any other assignment in the past twelve months.

PL or its associates might have received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months.

PL or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months

PL or its associates might have received any compensation or other benefits from the subject company or third party in connection with the research report.

PL encourages independence in research report preparation and strives to minimize conflict in preparation of research report. PL or its analysts did not receive any compensation or other benefits from the subject company or third party in connection with the preparation of the research report. PL or its Research Analysts do not have any material conflict of interest at the time of publication of this report.

It is confirmed that Mr. Surajit Pal (PGDBA, CFA, M.Com), Research Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

The Research analysts for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report.

The research analysts for this report has not served as an officer, director or employee of the subject company PL or its research analysts have not engaged in market making activity for the subject company

Our sales people, traders, and other professionals or affiliates may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest.

PL and its associates, their directors and employees may (a) from time to time, have a long or short position in, and buy or sell the securities of the subject company or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the subject company or act as an advisor or lender/borrower to the subject company or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.

DISCLAIMER/DISCLOSURES (FOR US CLIENTS)**ANALYST CERTIFICATION**

The research analysts, with respect to each issuer and its securities covered by them in this research report, certify that: All of the views expressed in this research report accurately reflect his or her or their personal views about all of the issuers and their securities; and No part of his or her or their compensation was, is or will be directly related to the specific recommendation or views expressed in this research report

Terms & conditions and other disclosures:

This research report is a product of Prabhudas Lilladher Pvt. Ltd., which is the employer of the research analyst(s) who has prepared the research report. The research analyst(s) preparing the research report is/are resident outside the United States (U.S.) and are not associated persons of any U.S. regulated broker-dealer and therefore the analyst(s) is/are not subject to supervision by a U.S. broker-dealer, and is/are not required to satisfy the regulatory licensing requirements of FINRA or required to otherwise comply with U.S. rules or regulations regarding, among other things, communications with a subject company, public appearances and trading securities held by a research analyst account.

This report is intended for distribution by Prabhudas Lilladher Pvt. Ltd. only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the U.S. Securities and Exchange Act, 1934 (the Exchange Act) and interpretations thereof by U.S. Securities and Exchange Commission (SEC) in reliance on Rule 15a-6(a)(2). If the recipient of this report is not a Major Institutional Investor as specified above, then it should not act upon this report and return the same to the sender. Further, this report may not be copied, duplicated and/or transmitted onward to any U.S. person, which is not the Major Institutional Investor.

In reliance on the exemption from registration provided by Rule 15a-6 of the Exchange Act and interpretations thereof by the SEC in order to conduct certain business with Major Institutional Investors, Prabhudas Lilladher Pvt. Ltd. has entered into an agreement with a U.S. registered broker-dealer, Marco Polo Securities Inc. ("Marco Polo").

Transactions in securities discussed in this research report should be effected through Marco Polo or another U.S. registered broker dealer.