Institutional Equity Research

Torrent Pharma

Pharmaceuticals | India

Event Update | October 10, 2019

CMP (Rs)	1,631
Upside/ (Downside) (%)	7
Bloomberg Ticker	TRP IN
Market Cap. (Rs bn)	276
Free Float (%)	29
Shares O/S (mn)	169.3

HOLD

Target Price: Rs1,740

US FDA Issues Warning Letter to Indrad Facility

The USFDA has issued a warning letter (WL) to Torrent Pharma's (TRP) Indrad (Gujarat) API and formulations facility. This WL is based on the Corrective & Preventive Action (CAPA) submitted by TRP to the observations raised by US FDA. The inspection was conducted in Apr'19 following which the US FDA issued four observations relating to deficiency i.e. Out of Specification (OOS) test results. Subsequently, the US FDA accorded Indrad facility as OAI (Official Action Indicated) status in Aug'19. Indrad is an important facility for TRP, as it contributes ~80% to its US sales. Currently, total of 34 products are pending for approvals. We expect new product approvals will be impacted in future until the plant gets regulatory clearance. We have not factored in any new launches in our valuation model. **We change our recommendation on the stock to HOLD from BUY with unrevised Target Price of Rs1,740, valuing it at 14x of FY21E EV/EBITDA.**

US – A Small Biz for TRP; Limited Impact of Regulatory Issues

The US business is a small business for TRP, which contributes ~20% of total sales. We note that TRP's other important Dahej facility also received OAI status in Jul'19 (5 observations; similar to Indrad facility). In most cases, OAI status converts into WL. So, Dahej plant is most likely to get WL in the near-term. Both plants are important from filing and new launches perspectives. In 1QFY20 earnings con-call, the management highlighted that in the worst-case scenario (delay in resolution of pending US FDA issues at Dahej and Indrad), it expects US sales to remain flat in FY20E (US$227mn in FY19) led by sales growth opportunities even in plain vanilla oral solid dosage (OSD) on account of frequent instances of shortages, product launches from external partners and ramp-up in existing products. Hence, we see these regulatory issues have limited impact on TRP's US business. We estimate TRP's US sales at US$212mn and US$224mn in FY20E and FY21E, respectively. We have already factored in US FDA pending issues at Dahej and Indrad facilities into our model in 1QFY20 only.

India Biz – Key Growth Driver

In our view, India business is a major growth driver for TRP considering high contribution (45% of sales). It grew by 12.6% YoY in 1QFY20, which is better than its peers. TRP is focusing on volume growth in FY20E, while it expects domestic business to grow faster than the IPM with focus on specialty prescription products. TRP also sees further margin improvement from cost synergy with the consolidation of Unichem business. Chronic segment (including sub-chronic) contributed ~75% to domestic sales (72% prescriptions from the specialists). We have seen strong improvement in field force productivity/MR/month since Unichem acquisition from Rs0.44mn in FY18 to Rs0.62mn in 4QFY19 to Rs0.72mn in 1QFY20. We expect domestic business to clock 12-13% CAGR over FY19-21 led by new launches.

Outlook & Valuation

TRP is a relatively safer play in current scenario due to higher revenue contribution from domestic business, while lower exposure to US offers comparatively better earnings visibility. We have already factored in US FDA pending issues at Dahej and Indrad facilities into our model in 1QFY20 only. Looking ahead, the Management sees strong growth across geographies except the US. At CMP, the stock trades at 15.0x and 13.3x of FY20E and FY21E EV/EBITDA, which offers limited upside potential. **Hence, we change our recommendation on the stock to HOLD from BUY with unrevised Target Price of Rs1,740, valuing it at 14x of FY21E EV/EBITDA.**

Risks to the View

- **Downside Risks:** Slower ramp-up in domestic business; and weak sales performance in other geographies.
- **Upside Risks:** Strong growth in domestic business; and early resolution of pending regulatory issues.

Share price (%)	1 mth	3 mth	12 mth
Absolute performance	(5.3)	4.9	2.8
Relative to Nifty	2.2	(2.9)	9.9

Shareholding Pattern (%)	Jun-19	Mar-19
Promoter	71.3	71.3
Public	28.8	28.8

Key Financials

(Rs mn)	FY19	FY20E	FY21E
Sales	76,730	84,684	93,204
EBITDA	19,833	21,190	23,261
Adj. PAT	7,934	7,854	9,528
EPS (Rs)	46.9	46.4	56.3
P/E (x)	34.8	35.1	29.0
EV/Sales (x)	4.3	3.8	3.3
EV/EBITDA (x)	16.6	15.1	13.4
ROE (%)	16.8	15.2	16.5
ROCE (%)	13.2	14.0	15.5
Margin (%)	25.8	25.0	25.0

1 Year Stock Price Performance

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Profit & Loss Statement

Y/E March (Rs mn)	FY18	FY19	FY20E	FY21E
Net sales	**60,021**	**76,730**	**84,684**	**93,204**
% yoy change	2.5	27.8	10.4	10.1
RM cost	16,735	22,198	23,946	26,417
Employee expenses	11,353	14,040	15,667	17,243
Other expenses	18,441	20,660	23,881	26,284
Total operating expenditure	**46,529**	**56,898**	**63,494**	**69,944**
EBIDTA	**13,492**	**19,833**	**21,190**	**23,261**
EBIDTA margin (%)	22.5	25.8	25.0	25.0
Depreciation	4,086	6,177	6,489	6,648
Other income	2,988	570	508	466
EBIT	**12,395**	**14,226**	**15,209**	**17,078**
Interest costs	3,085	5,038	4,736	4,374
PBT	**9,310**	**9,188**	**10,473**	**12,704**
Taxes	2,529	1,254	2,618	3,176
Tax rate (%)	27.2	13.6	25.0	25.0
Adj PAT	**6,781**	**7,934**	**7,854**	**9,528**
% yoy change	-27.4	17.0	-1.0	21.3
Exceptional item	-	3,570	-	-
Reported PAT	**6,781**	**4,364**	**7,854**	**9,528**
% yoy change	-27.4	-35.6	80.0	21.3
Adj EPS (Rs)	**40.1**	**46.9**	**46.4**	**56.3**

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Balance Sheet

Y/E March (Rs mn)	FY18	FY19	FY20E	FY21E
SOURCES OF FUNDS				
Equity Share Capital	846	846	846	846
Reserves & Surplus	45,376	46,397	50,866	57,009
Shareholders Funds	46,222	47,243	51,712	57,855
Minority Interest	5	-	0	1
Total Loans	64,623	60,381	56,381	52,381
Other long term liabilities	202	223	223	223
Deferred tax liability	0	75	75	75
Total Liabilities	**111,052**	**107,922**	**108,392**	**110,535**
APPLICATION OF FUNDS				
Gross Block	92,747	97,384	99,834	102,284
Less: Acc. Depreciation	15,948	21,877	28,366	35,015
Net Block	76,799	75,507	71,468	67,269
Capital Work-in-Progress	8,217	8,141	9,191	10,241
Investments	1	21	21	21
Current Assets	52,624	50,375	57,389	66,477
Current invetsment	4,923	3,514	3,584	3,655
Inventories	19,663	19,352	19,761	21,809
Sundry Debtors	12,535	14,357	15,845	17,440
Cash and cash equivalents	2,411	5,888	10,416	15,236
Bank balances other than cash and cash equivalents	6,261	2,273	2,273	2,273
Loans and Advances	31	38	42	46
Other Current Assets	6,800	4,955	5,469	6,019
Current liabilities	31,380	33,286	36,737	40,433
Net Current Assets	**21,244**	**17,089**	**20,652**	**26,044**
Deferred tax assets	2,759	3,699	3,699	3,699
Other non-current assets	2,032	3,465	3,361	3,261
Total Assets	**111,052**	**107,922**	**108,392**	**110,535**

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Cash Flow Statement

Y/E March (Rs mn)	FY18	FY19	FY20E	FY21E
Profit before tax	9,310	5,617	10,473	12,704
Depreciation	4,086	6,177	6,489	6,648
Interest provided	3,085	5,038	4,736	4,374
Change in Working Capital	(3,601)	993	965	(573)
Tax Paid	(2,836)	(2,812)	(2,618)	(3,176)
Others	(1,102)	2,968	-	-
Cash Flow from Operations	**8,942**	**17,981**	**20,045**	**19,978**
(Inc.)/ Dec. in Fixed Assets	(7,913)	(6,628)	(3,500)	(3,500)
(Inc.)/ Dec. in Investments	(273)	3,676	-	-
Acquisition of business / undertaking	(39,619)	-	-	-
Others	734	539	104	101
Cash Flow from Investing	**(47,070)**	**(2,413)**	**(3,396)**	**(3,399)**
Issue of Equity	-	-	-	-
Inc./(Dec.) in loans	39,579	(5,013)	(4,000)	(4,000)
Dividend Paid (Incl. Tax)	(2,648)	(3,097)	(3,385)	(3,385)
Interest provided	(2,758)	(5,035)	(4,736)	(4,374)
Others	-	-	-	-
Cash Flow from Financing	**34,174**	**(13,145)**	**(12,121)**	**(11,759)**
Inc./(Dec.) in Cash and cash equivalents	(3,954)	2,423	4,528	4,820
Effect of exchange rate changes and others	299	(41)	-	-
Cash and cash equivalents at beginning of year	**10,675**	**7,020**	**9,401**	**13,930**
Cash and cash equivalents at end of year	**7,020**	**9,401**	**13,930**	**18,749**
Cash and cash equivalents	2,411	5,888	10,416	15,236
Current investments in mutual funds	4,609	3,514	3,514	3,514

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Key Ratios

Y/E March	FY18	FY19	FY20E	FY21E
Valuation Ratio (x)				
P/E	40.7	34.8	35.1	29.0
P/CEPS	25.4	19.6	19.2	17.1
P/BV	6.0	5.8	5.3	4.8
Dividend yield (%)	1.0	1.1	1.2	1.2
EV/Sales	5.5	4.3	3.8	3.3
EV/EBITDA	24.6	16.6	15.1	13.4
Per Share Data (Rs)				
EPS	40.1	46.9	46.4	56.3
Cash EPS	64.2	83.4	84.7	95.6
DPS	16.9	18.3	20.0	20.0
Book Value (BV)	273.1	279.1	305.5	341.8
Returns (%)				
RoCE	11.2	13.2	14.0	15.5
RoE	14.7	16.8	15.2	16.5
Turnover ratios (x)				
Asset Turnover (Gross Block)	0.6	0.8	0.8	0.9
Asset Turnover (Net Block)	0.8	1.0	1.2	1.4
Inventory (days)	120	92	94	94
Receivables (days)	76	68	68	68
Payables (days)	153	125	125	125
Cash conversion cycle (days)	42	35	37	37

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Rating History

Date	Reco	CMP	TP
24-July-19	HOLD	1,468	1,740
21-May-19	HOLD	1,600	1,625
31-Jan-19	HOLD	1,845	1,860
05-Nov-18	BUY	1631	1870
03-Aug-18	BUY	1628	1870
01-Jun-18	BUY	1454	1630
19-Feb-18	BUY	1395	1570
13-Nov-17	BUY	1222	1450

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Rating Guides

Rating	Expected absolute returns (%) over 12 months
BUY	>10%
HOLD	-5% to 10%
REDUCE	>-5%

NAVEEN KULKARNI

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