

January 10, 2019

## Company Report

■ Change in Estimates | ■ Target | ■ Reco

### Change in Estimates

	Current		Previous	
	FY20E	FY21E	FY20E	FY21E
Rating	BUY		BUY	
Target Price	994		994	
Sales (Rs. m)	210,857	228,879	210,857	228,879
% Chng.	-	-	-	-
EBITDA (Rs. m)	47,021	49,896	47,021	49,896
% Chng.	-	-	-	-
EPS (Rs.)	55.2	58.1	55.2	58.1
% Chng.	-	-	-	-

### Key Financials

	FY18	FY19E	FY20E	FY21E
Sales (Rs. m)	162,329	189,379	210,857	228,879
EBITDA (Rs. m)	35,216	42,231	47,021	49,896
Margin (%)	21.7	22.3	22.3	21.8
PAT (Rs. m)	23,952	29,138	32,366	34,034
EPS (Rs.)	40.9	49.7	55.2	58.1
Gr. (%)	4.1	21.6	11.1	5.2
DPS (Rs.)	-	4.5	4.5	4.5
Yield (%)	-	0.6	0.6	0.6
RoE (%)	22.8	22.3	20.3	18.0
RoCE (%)	20.5	20.7	20.2	18.8
EV/Sales (x)	3.0	2.6	2.3	2.1
EV/EBITDA (x)	13.7	11.5	10.2	9.5
PE (x)	18.8	15.5	13.9	13.3
P/BV (x)	3.9	3.1	2.6	2.2

### Key Data

ARBN.BO | ARBP IN

52-W High / Low	Rs.830 / Rs.527
Sensex / Nifty	36,010 / 10,795
Market Cap	Rs.451bn / \$ 6,395m
Shares Outstanding	586m
3M Avg. Daily Value	Rs.4360.38m

### Shareholding Pattern (%)

Promoter's	51.87
Foreign	19.11
Domestic Institution	15.04
Public & Others	13.98
Promoter Pledge (Rs bn)	5.19

### Stock Performance (%)

	1M	6M	12M
Absolute	4.8	26.4	14.1
Relative	2.3	27.3	9.4

### Surajit Pal

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## Pfizer plant closures to benefit TazoPip, penems

We believe ARBP is likely to benefit from Pfizer's rationalization of two injectable plants in India, which are key contributors in limited competition drugs, Tazo+Pip and Penems. We expect ARBP's revenue from these drugs to gradually increase over years as Injectables being hospital products, expand market share when new tender floats materialize from large GPOs in US. ARBP trades at PE of 15.4x and 13.9x of FY19E and FY20E respectively, one of the few inexpensive valuation in pharma sector. At our TP of Rs994, the stock trades at PE 20x and 18x of FY19E and FY20E, respectively. Maintain 'Buy'.

### Pfizer to close down Chennai and Aurangabad Units

- Media news:** Pfizer plans to shut down two plants in Chennai (Irrungattukottai) and Aurangabad in India post cost-benefit evaluation of plant infrastructure in India. Hospira acquired these two plants from Orchid Pharmaceuticals and later, these came into Pfizer's fold from acquisition of Hospira in February 2015. Hospira bought the two plants to facilitate its long standing manufacturing issues with USFDA for its Rocky Mount plant in US, which disrupted its injectable business leading to shortages in Tazo+Pip.
- Genesis of the plants:** With chequered regulatory history since 2013, Pfizer management evaluated that the issues of manufacturing quality are beyond redemption especially after the USFDA's Warning Letter (WL) with 11 observations (including repeat of 8 observations). This has led to long-term loss of product demand in key geographies as it interrupts the operating schedule of productions in its network of plants.

While Aurangabad plant produces API, the Chennai plant was exclusively for a portfolio of sterile Injectables in cephalosporin and betalactum molecules with a separate block for production of penems. Along with key cephalosporin Injectables, the Chennai plant supplies global requirements of generic Tazo+Pip (combination of Tazobactam and Piperacillin), meropenem and imipenem combinations in the Established Products division of Pfizer.

### How it benefits Aurobindo

- Pfizer will take 12-18 months to restore supply:** With rationalization of the two plants, ARBP's benefit through the expansion of Rx share (**Tazo+Pip**) will continue for longer term as Pfizer's reinstatement of the loss of supply (for US and EU markets, including regulatory approvals), will require minimum 12 months. The Chennai plant stopped production for US market since June 2018 post USFDA Warning Letter (WL), while Pfizer continued supply of Tazo-Pip at lower quantity from captive plant in US.

- **Aurobindo to gain Share:** While a significant part of Pfizer's Rx share (28-33%) will be up for grab among the five US generic players, ARBP will leverage its market leadership in Tazo+Pip (Rx share 55-58%) to obtain a large part of Pfizer's loss of market share. We expect ARBP's Rx share continues to expand with commissioning (June 2017) of Unit-16 (a new betalactum plant), which operates at 10% capacity utilization. Tazo+Pip contributed revenues of US\$35m in FY18 and is expected to increase to US\$45m in FY19E with revenues of US\$3-4m per month currently. (Expected EBITDA margin of over 50%).
- **Unit-16: New plant for betalactum products**—ARBP commissioned (June 2017) the new injectable plant in Hyderabad for betalactum products such as Tazo+Pip. With current operation at 10% capacity utilisation, the new plant is poised to meet the production of additional demand for Tazo+Pip post closure of the Chennai plant by Pfizer. With key regulatory approvals in hand, the Unit-16 currently produces only Tazo-Pip for US market and plans to expand betalactum product pipeline for US, EU and other semi-reg markets. ARBP currently produces major part of US and EU supply of Tazo+Pip and other betalactum products in Unit-12, though headroom for additional capacity is limited. This has resulted in investment for new Unit-16 as ARBP plans for target volume push for betalactum products such as Tazo+Pip both in US and EU markets.
- **AuroNext (SBU for venture in Penems)**—The closure of the Chennai plant will help ARBP to expand its benefits of sole generic in Ertapenem as well as reduce further competition in Meropenem to three large generic players in US. ARBP has approval and marketed two penems, Meropenem and Ertapenem. Rest of its application for other penems (Doripenem and Imipenem/cilastatin) are withdrawn due to minor market opportunity in comparison to the number of existing competitors.
- ARBP launched Meropenem in April 2017 and contributed US\$23m revenues in FY18. It launched Ertapenem in July 2018 on day-1 generic competition. There is one AG along with originator (MSD) while other approved generic (ACS Dobfar) has not launched yet due to manufacturing issues with USFDA. Pfizer being large competitor in penem products, the closure of Chennai plant will delay the prospect of its approval in Ertapenem till it re-submit ANDA with shift of manufacturing plant. Pfizer's Rx share of 13-14% in Meropenem and unused capacity in Auronext plant, it will offer opportunity for ARBP to expand Rx share in Meropenem (gMerrem).

With revenues of US\$2m per month in meropenem, we expect ARBP's revenues from penem to be US\$65m including revenues of Ertapenem at US\$40m and Meropenem at US\$25m in FY19E.

#### **Exhibit 1: Betalactum, Penem key drugs opportunity in US**

<b>Molecule</b>	<b>US mkt size (US\$ m)</b>	<b>ARBP Rx share (%)</b>	<b>Pfizer Rx share (%)</b>
TazoPip	230	55-58	28-33
Meropenem	100	11-13	13-14
Doripenem	8	NA	NA
Imipenem/Cilastatin	20	NA	NA

Source: Company, PL

## Financials

### Income Statement (Rs m)

Y/e Mar	FY18	FY19E	FY20E	FY21E
<b>Net Revenues</b>	<b>162,329</b>	<b>189,379</b>	<b>210,857</b>	<b>228,879</b>
YoY gr. (%)	9.4	16.7	11.3	8.5
Cost of Goods Sold	67,527	81,338	90,563	98,303
Gross Profit	94,801	108,041	120,294	130,575
Margin (%)	58.4	57.1	57.1	57.1
Employee Cost	21,308	21,305	23,721	25,749
Other Expenses	6,669	11,363	12,651	14,877
<b>EBITDA</b>	<b>35,216</b>	<b>42,231</b>	<b>47,021</b>	<b>49,896</b>
YoY gr. (%)	10.4	19.9	11.3	6.1
Margin (%)	21.7	22.3	22.3	21.8
Depreciation and Amortization	5,580	6,568	7,397	8,476
<b>EBIT</b>	<b>29,636</b>	<b>35,663</b>	<b>39,624</b>	<b>41,419</b>
Margin (%)	18.3	18.8	18.8	18.1
Net Interest	777	1,021	941	775
Other Income	3,690	3,911	4,146	4,394
<b>Profit Before Tax</b>	<b>32,548</b>	<b>38,553</b>	<b>42,829</b>	<b>45,038</b>
Margin (%)	20.1	20.4	20.3	19.7
Total Tax	8,463	9,445	10,493	11,034
Effective tax rate (%)	26.0	24.5	24.5	24.5
<b>Profit after tax</b>	<b>24,086</b>	<b>29,108</b>	<b>32,336</b>	<b>34,004</b>
Minority interest	(34)	(30)	(30)	(30)
Share Profit from Associate	-	-	-	-
<b>Adjusted PAT</b>	<b>23,952</b>	<b>29,138</b>	<b>32,366</b>	<b>34,034</b>
YoY gr. (%)	4.1	21.6	11.1	5.2
Margin (%)	14.8	15.4	15.3	14.9
Extra Ord. Income / (Exp)	-	-	-	-
<b>Reported PAT</b>	<b>23,952</b>	<b>29,138</b>	<b>32,366</b>	<b>34,034</b>
YoY gr. (%)	4.1	21.6	11.1	5.2
Margin (%)	14.8	15.4	15.3	14.9
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	23,952	29,138	32,366	34,034
<b>Equity Shares O/s (m)</b>	<b>586</b>	<b>586</b>	<b>586</b>	<b>586</b>
<b>EPS (Rs)</b>	<b>40.9</b>	<b>49.7</b>	<b>55.2</b>	<b>58.1</b>

Source: Company Data, PL Research

### Balance Sheet Abstract (Rs m)

Y/e Mar	FY18	FY19E	FY20E	FY21E
<b>Non-Current Assets</b>				
<b>Gross Block</b>	<b>70,638</b>	<b>95,469</b>	<b>116,341</b>	<b>131,841</b>
Tangibles	59,555	81,550	100,047	113,347
Intangibles	11,083	13,918	16,294	18,494
<b>Acc: Dep / Amortization</b>	<b>13,597</b>	<b>20,165</b>	<b>27,562</b>	<b>36,039</b>
Tangibles	12,189	17,722	23,969	31,209
Intangibles	1,407	2,443	3,593	4,830
<b>Net fixed assets</b>	<b>57,041</b>	<b>75,303</b>	<b>88,779</b>	<b>95,803</b>
Tangibles	47,366	63,829	76,078	82,138
Intangibles	9,676	11,475	12,701	13,665
Capital Work In Progress	15,830	11,873	6,500	6,500
Goodwill	8,165	8,165	8,165	8,165
Non-Current Investments	4,044	4,276	4,567	4,930
Net Deferred tax assets	(765)	1,568	2,852	4,204
Other Non-Current Assets	2,504	3,130	3,913	4,891
<b>Current Assets</b>				
Investments	0	0	0	0
Inventories	58,584	61,993	65,788	69,908
Trade receivables	30,844	32,687	36,395	43,895
Cash & Bank Balance	12,616	5,715	6,119	7,787
Other Current Assets	11,790	12,969	14,266	15,693
<b>Total Assets</b>	<b>211,052</b>	<b>227,319</b>	<b>247,425</b>	<b>272,322</b>
<b>Equity</b>				
Equity Share Capital	586	586	586	586
Other Equity	116,218	144,030	173,311	204,260
<b>Total Network</b>	<b>116,804</b>	<b>144,615</b>	<b>173,897</b>	<b>204,846</b>
<b>Non-Current Liabilities</b>				
Long Term borrowings	4,512	2,256	1,128	564
Provisions	559	698	873	1,091
Other non current liabilities	-	-	-	-
<b>Current Liabilities</b>				
ST Debt / Current of LT Debt	40,313	36,413	33,113	28,146
Trade payables	26,274	28,018	27,729	30,099
Other current liabilities	20,218	14,153	9,550	6,471
<b>Total Equity &amp; Liabilities</b>	<b>211,052</b>	<b>227,319</b>	<b>247,425</b>	<b>272,322</b>

Source: Company Data, PL Research

**Cash Flow (Rs m)**

Y/e Mar	FY18	FY19E	FY20E	FY21E
PBT	32,548	38,553	42,829	45,038
Add. Depreciation	5,580	6,568	7,397	8,476
Add. Interest	777	1,021	941	775
Less Financial Other Income	3,690	3,911	4,146	4,394
Add. Other	(1,582)	(472)	(1,254)	(1,474)
Op. profit before WC changes	37,323	45,670	49,913	52,815
Net Changes-WC	(10,405)	(11,042)	(14,042)	(14,160)
Direct tax	(8,267)	(10,602)	(11,778)	(12,386)
<b>Net cash from Op. activities</b>	<b>18,650</b>	<b>24,026</b>	<b>24,093</b>	<b>26,270</b>
Capital expenditures	(19,596)	(20,873)	(15,500)	(15,500)
Interest / Dividend Income	158	161	164	167
Others	(657)	-	-	-
<b>Net Cash from Inv. activities</b>	<b>(20,095)</b>	<b>(20,712)</b>	<b>(15,336)</b>	<b>(15,333)</b>
Issue of share cap. / premium	-	-	-	-
Debt changes	11,184	(6,156)	(4,428)	(5,531)
Dividend paid	-	(3,085)	(3,085)	(3,085)
Interest paid	(777)	(1,021)	(941)	(775)
Others	-	-	-	-
<b>Net cash from Fin. activities</b>	<b>10,407</b>	<b>(10,262)</b>	<b>(8,453)</b>	<b>(9,391)</b>
<b>Net change in cash</b>	<b>8,963</b>	<b>(6,947)</b>	<b>304</b>	<b>1,547</b>
Free Cash Flow	(945)	3,154	8,593	10,770

Source: Company Data, PL Research

**Quarterly Financials (Rs m)**

Y/e Mar	Q4FY18	Q1FY19	Q2FY19	Q3FY19
<b>Net Revenue</b>	<b>39,886</b>	<b>41,816</b>	<b>46,671</b>	<b>47,473</b>
YoY gr. (%)	11.3	15.5	7.2	11.2
Raw Material Expenses	16,695	19,073	20,429	20,651
Gross Profit	23,192	22,743	26,242	26,822
Margin (%)	58.1	54.4	56.2	56.5
<b>EBITDA</b>	<b>7,436</b>	<b>7,105</b>	<b>9,417</b>	<b>9,666</b>
YoY gr. (%)	(22.4)	(4.4)	32.5	2.6
Margin (%)	18.6	17.0	20.2	20.4
Depreciation / Depletion	1,566	1,545	1,637	1,653
<b>EBIT</b>	<b>5,869</b>	<b>5,560</b>	<b>7,780</b>	<b>8,013</b>
Margin (%)	14.7	13.3	16.7	16.9
Net Interest	247	295	354	347
Other Income	884	443	708	770
<b>Profit before Tax</b>	<b>6,506</b>	<b>5,707</b>	<b>8,135</b>	<b>8,436</b>
Margin (%)	16.3	13.6	17.4	17.8
Total Tax	1,224	1,155	1,754	1,856
Effective tax rate (%)	18.8	20.2	21.6	22.0
<b>Profit after Tax</b>	<b>5,282</b>	<b>4,552</b>	<b>6,380</b>	<b>6,580</b>
Minority interest	(3)	(5)	(2)	(2)
Share Profit from Associates	-	-	-	-
<b>Adjusted PAT</b>	<b>5,285</b>	<b>4,557</b>	<b>6,383</b>	<b>6,582</b>
YoY gr. (%)	(0.7)	(12.1)	(18.3)	10.6
Margin (%)	13.3	10.9	13.7	13.9
Extra Ord. Income / (Exp)	-	-	-	-
<b>Reported PAT</b>	<b>5,285</b>	<b>4,557</b>	<b>6,383</b>	<b>6,582</b>
YoY gr. (%)	(0.7)	(12.1)	(18.3)	10.6
Margin (%)	13.3	10.9	13.7	13.9
Other Comprehensive Income	-	-	-	-
<b>Total Comprehensive Income</b>	<b>5,285</b>	<b>4,557</b>	<b>6,383</b>	<b>6,582</b>
Avg. Shares O/s (m)	586	586	586	586
<b>EPS (Rs)</b>	<b>9.0</b>	<b>7.8</b>	<b>10.9</b>	<b>11.2</b>

Source: Company Data, PL Research

**Key Financial Metrics**

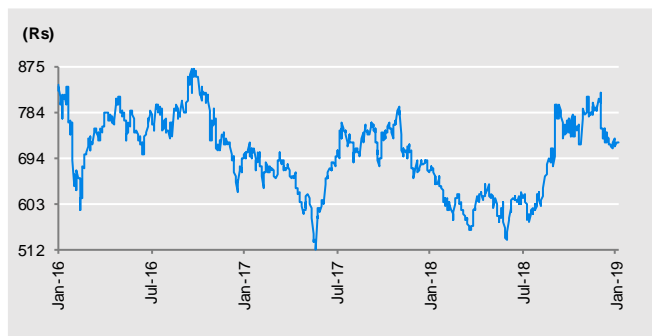
Y/e Mar	FY18	FY19E	FY20E	FY21E
<b>Per Share(Rs)</b>				
EPS	40.9	49.7	55.2	58.1
CEPS	50.4	60.9	67.9	72.6
BVPS	199.4	246.8	296.8	349.6
FCF	(1.6)	5.4	14.7	18.4
DPS	-	4.5	4.5	4.5
<b>Return Ratio(%)</b>				
RoCE	20.5	20.7	20.2	18.8
ROIC	14.9	16.1	16.4	15.7
RoE	22.8	22.3	20.3	18.0
<b>Balance Sheet</b>				
Net Debt : Equity (x)	0.3	0.2	0.2	0.1
Net Working Capital (Days)	142	128	129	133
<b>Valuation(x)</b>				
PER	18.8	15.5	13.9	13.3
P/B	3.9	3.1	2.6	2.2
P/CEPS	15.3	12.6	11.3	10.6
EV/EBITDA	13.7	11.5	10.2	9.5
EV/Sales	3.0	2.6	2.3	2.1
Dividend Yield (%)	-	0.6	0.6	0.6

Source: Company Data, PL Research

**Key Operating Metrics (Rs m)**

Y/e Mar	FY18	FY19E	FY20E	FY21E
US Formulations	76,921	91,122	103,098	113,408
EU & ROW	43,536	51,220	57,562	62,899
ARV formulations	13,276	15,728	17,795	19,574
APIs	29,151	31,282	32,375	32,969

Source: Company Data, PL Research

**Price Chart**
**Recommendation History**


No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	13-Apr-18	BUY	909	620
2	21-May-18	BUY	909	595
3	27-Jun-18	BUY	909	608
4	10-Jul-18	BUY	909	627
5	1-Aug-18	BUY	909	600
6	11-Aug-18	BUY	909	611
7	6-Sep-18	BUY	909	759
8	5-Oct-18	BUY	909	757
9	13-Nov-18	BUY	909	796
10	7-Jan-19	BUY	994	725

**Analyst Coverage Universe**

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Aurobindo Pharma	BUY	994	725
2	Cadila Healthcare	Accumulate	371	349
3	Cipla	Reduce	415	514
4	Dr. Lal PathLabs	Accumulate	1,009	948
5	Dr. Reddy's Laboratories	Reduce	2,170	2,559
6	Eris Lifesciences	Accumulate	704	667
7	Glenmark Pharmaceuticals	Reduce	528	654
8	Indoco Remedies	Reduce	103	217
9	Ipca Laboratories	BUY	899	784
10	Jubilant Life Sciences	Accumulate	829	710
11	Lupin	Reduce	713	820
12	Sun Pharmaceutical Industries	Reduce	464	431
13	Thyrocare Technologies	BUY	795	541

**PL's Recommendation Nomenclature (Absolute Performance)**

<b>Buy</b>	: > 15%
<b>Accumulate</b>	: 5% to 15%
<b>Hold</b>	: +5% to -5%
<b>Reduce</b>	: -5% to -15%
<b>Sell</b>	: < -15%
<b>Not Rated (NR)</b>	: No specific call on the stock
<b>Under Review (UR)</b>	: Rating likely to change shortly



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