

Granules India

| | |
|-----------------------|--------------------|
| BSE SENSEX | S&P CNX |
| 34,006 | 10,455 |
| Bloomberg | GRAN IN |
| Equity Shares (m) | 229 |
| M.Cap.(INRb)/(USDb) | 30.9 / 0.5 |
| 52-Week Range (INR) | 157 / 102 |
| 1, 6, 12 Rel. Per (%) | -13/0/-29 |
| Avg Val, INRm | 295.0 |
| Free float (%) | 55.1 |

Financials & Valuations (INR b)

| Y/E Mar | 2018E | 2019E | 2020E |
|-------------|-------|-------|-------|
| Net Sales | 16.4 | 21.6 | 27.1 |
| EBITDA | 3.0 | 4.2 | 5.5 |
| PAT | 1.5 | 2.0 | 2.8 |
| EPS (INR) | 6.3 | 7.9 | 11.0 |
| Gr. (%) | -12.4 | 25.2 | 38.7 |
| BV/Sh (INR) | 54.6 | 59.9 | 67.0 |
| RoE (%) | 13.2 | 13.9 | 17.4 |
| RoCE (%) | 13.9 | 14.7 | 18.1 |
| P/E (x) | 18.8 | 15.0 | 10.8 |
| P/BV (x) | 2.2 | 2.0 | 1.8 |

Estimate change



TP change



Rating change



CMP: INR119

TP: INR175(+47%)

Buy

Revenue in-line; margins below expectation

- Sales rose 14% YoY to INR4.1b (est. of INR4.06b). EBITDA margin came in at 18% (-320bp YoY, -160 bp QoQ) v/s our expectation of 20.6%, because of: 1) high input cost, 2) forex fluctuations and 3) new capacity ramp-up. EBITDA stood at INR740m v/s our estimate of INR837m. PAT declined 10% YoY to INR350m due to lower margins and associate income (est. of INR433m).
- **US business – Methergene approval will be key:** GRAN plans to file ~20 ANDAs in the US until FY19. Of these, ~50% complex ANDAs will be filed from its US-based Virginia facility and the rest from its India facility in Gagilapur. It has already filed two complex generic ANDAs, including Methergene (LPC is the innovator; market size: ~USD50-60m). GRAN is the only generic filer, and an approval is expected over the next few months.
- **Concall takeaways:** 1) In 3QFY18, Virginia facility was inspected for the first time by the USFDA with one 483, to which GRAN responded and also later received EIR. 2) On target to file 10 ANDAs in FY18; 5 ANDAs in 4Q (all complex ANDAs). 3) Maintained revenue guidance, although PAT may be impacted by lower margin; 4) First product from Virginia facility will be launched in 1QFY19. 5) Depreciation will increase from FY19, led by new facility becoming operational.
- **Stock trading at 15x FY19E EPS; US biz ramp-up key growth driver:** GRAN trades at 15x FY19E EPS (despite assuming >10% equity dilution). We believe the stock is poised for multiple re-rating on the back of asset sweating in traditional business, entry in high-value US business and commencement of API sales from Omnicem JV. We maintain our **Buy** rating with a TP of INR175 @18x 1HFY20E (v/s INR200 @ 18x 1HFY20E). We have cut our FY18E/19E/20E EPS by 8%/13%/17%, as we factor in the impact of loss of sales in JV business and lower margins.

Quarterly Performance

| Y/E March (Consolidated) | FY17 | | | | FY18E | | | | FY17 | FY18E | Est. | Var. |
|--------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|--------|--------|-------|--------|
| | 1Q | 2Q | 3Q | 4Q | 1Q | 2Q | 3Q | 4QE | | | 3QE | vs Est |
| Net Sales | 3,498 | 3,638 | 3,595 | 3,634 | 3,860 | 3,926 | 4,107 | 4,142 | 14,353 | 16,035 | 4,062 | 1.1% |
| YoY Change (%) | 8.4 | 3.1 | 4.2 | -2.4 | 10.3 | 7.9 | 14.3 | 14.0 | 0.4 | 11.7 | 13.0 | |
| Total Expenditure | 2,813 | 2,896 | 2,832 | 2,848 | 3,090 | 3,156 | 3,367 | 3,382 | 11,364 | 12,996 | 3,225 | |
| EBITDA | 685 | 742 | 763 | 785 | 769 | 769 | 740 | 760 | 2,988 | 3,039 | 837 | -11.5% |
| Margins (%) | 19.6 | 20.4 | 21.2 | 21.6 | 19.9 | 19.6 | 18.0 | 18.3 | 20.8 | 19.0 | 20.6 | |
| Depreciation | 163 | 185 | 187 | 180 | 176 | 186 | 196 | 204 | 715 | 762 | 250 | |
| Interest | 79 | 83 | 84 | 77 | 82 | 104 | 82 | 90 | 323 | 359 | 90 | |
| Other Income | 30 | 39 | 43 | 0 | 4 | 68 | 9 | 59 | 99 | 140 | 35 | |
| PBT before EO expense | 472 | 513 | 535 | 529 | 515 | 547 | 471 | 525 | 2,050 | 2,058 | 532 | -11.6% |
| Tax | 154 | 156 | 176 | 166 | 177 | 193 | 169 | 181 | 652 | 720 | 144 | |
| Rate (%) | 32.5 | 30.4 | 32.9 | 31.4 | 34.4 | 35.2 | 35.9 | 34.5 | 31.8 | 35.0 | 27.0 | |
| Minority Interest & Profit/Los | -71 | -51 | -31 | -94 | -30 | -49 | -49 | -48 | -247 | -175 | -45 | |
| PAT (Ex associate income) | 319 | 357 | 359 | 363 | 338 | 355 | 302 | 344 | 1,398 | 1,338 | 388 | -22.4% |
| Reported PAT | 390 | 408 | 390 | 457 | 368 | 403 | 350 | 391 | 1,645 | 1,513 | 433 | -19.2% |
| YoY Change (%) | 33.8 | 28.1 | 43.5 | 13.4 | -5.5 | -1.2 | -10.1 | -14.4 | 44.3 | -8.1 | 11.2 | |
| Margins (%) | 11.1 | 11.2 | 10.8 | 12.6 | 9.5 | 10.3 | 8.5 | 9.4 | 11.5 | 9.4 | 10.7 | |

E: MOSL Estimates

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Story in Charts

Exhibit 1: Revenues exhibited 14% YoY growth in 3QFY18

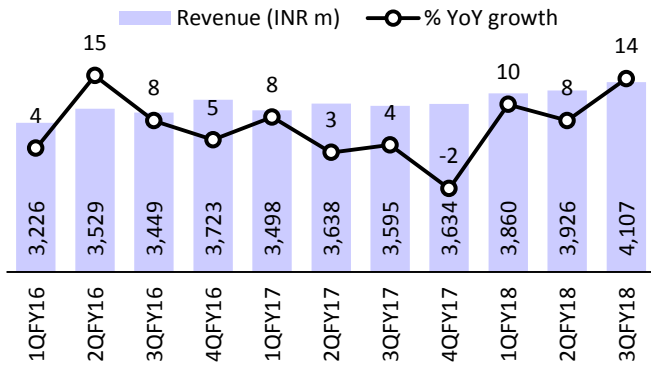


Exhibit 2: EBITDA margin declined 320bp YoY

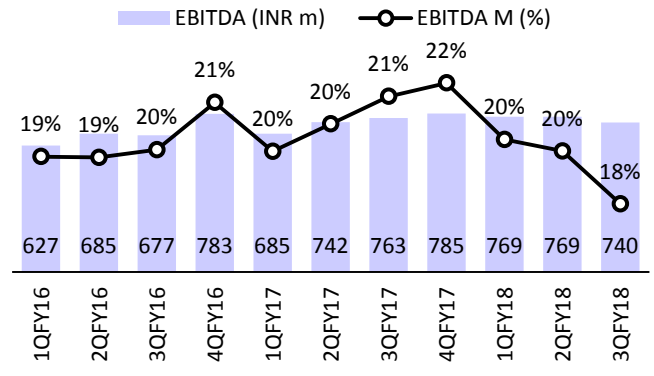


Exhibit 3: Revenues to exhibit 29% CAGR over FY18-20E

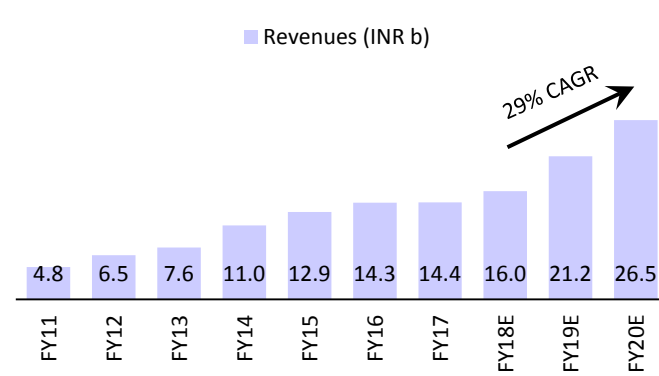


Exhibit 4: Formulation contribution to increase

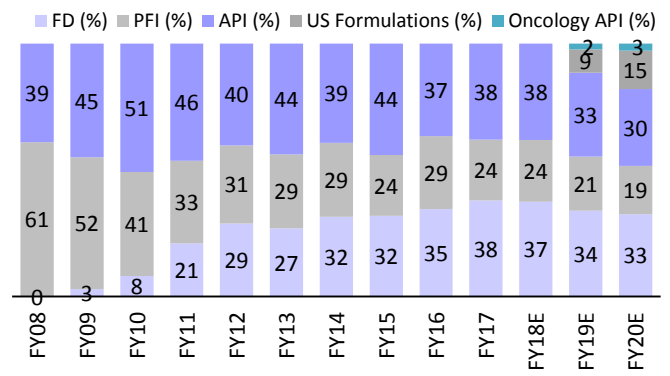


Exhibit 5: EBITDA margins to expand to 21% by FY20E

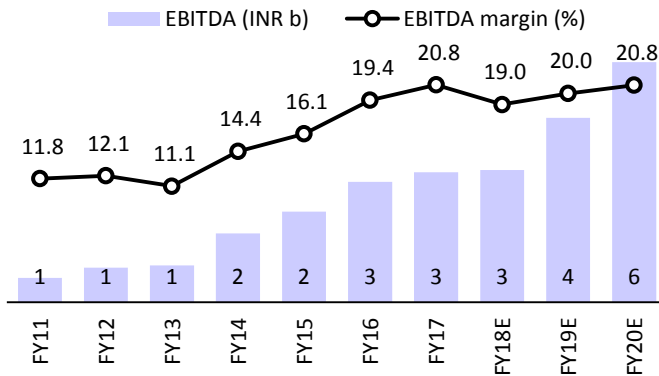


Exhibit 6: Geographical revenue break-up

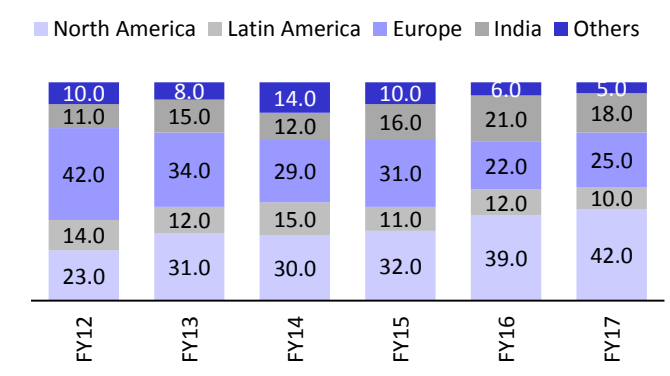
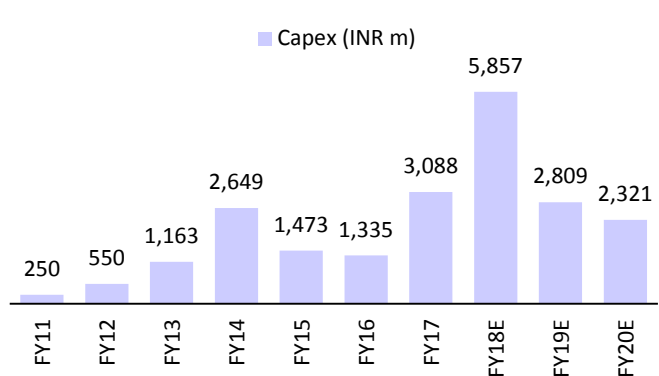
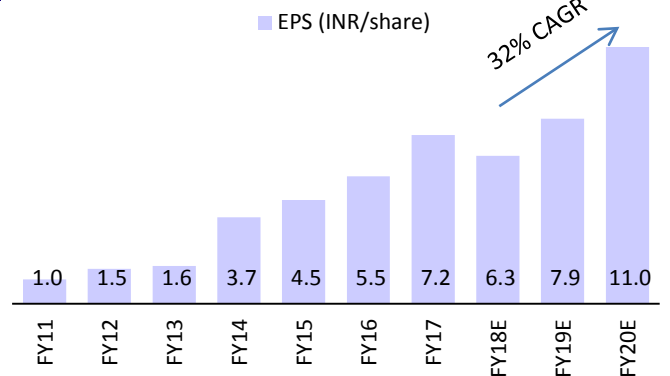


Exhibit 7: Capex to taper down FY19E onwards



Source: Company, MOSL

Exhibit 8: Earnings to exhibit 32% CAGR over FY18-20E



Source: Company, MOSL

Valuation and view

Over the last six years, GRAN reported 39% earnings CAGR on improved profitability, higher operating leverage and superior business mix. It expanded its finished dosages business at a CAGR of 24% over FY12-17, leading to higher profitability and improved utilization of the existing capacity of 18b tablets. Profitability of the PFI business has also improved substantially, with the implementation of 6MT order capacity. As a result, GRAN has expanded its EBITDA margins from 11.8% in FY11 to ~21% in FY17.

GRAN trades at 15x FY19E EPS (despite assuming >10% equity dilution). We believe the stock is poised for multiple re-rating on the back of asset sweating in traditional business, entry in high-value US business and commencement of API sales from Omnicem JV. We maintain our Buy rating with a TP of INR175 @18x 1HFY20E (v/s INR200 @ 18x 1HFY20E). We have cut our FY18E/19E/20E EPS by 8%/13%/17%, as we factor in the impact of loss of sales in JV business and lower margins.

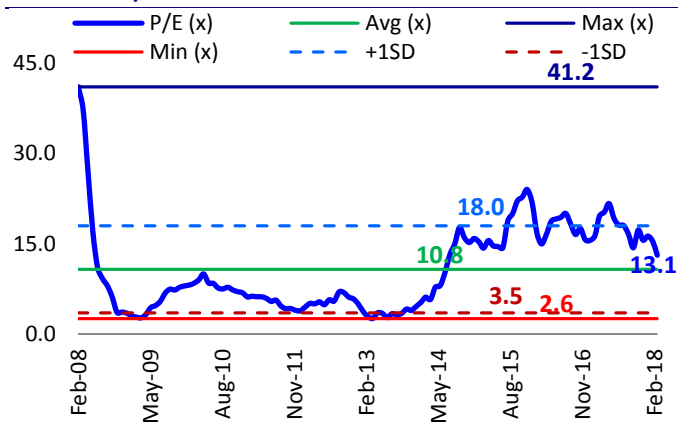
Key catalysts to drive stock’s performance over the medium term

- Finished dosages product approvals from regulated markets
- Commercialization of new capacity
- Higher-than-expected realizations from Omnicem JV

Risks to our investment thesis

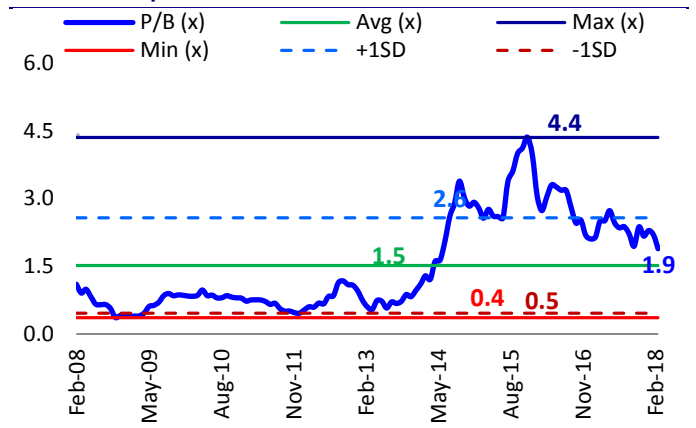
- Pricing pressure on existing products
- Regulatory risks related to already approved manufacturing facilities

Exhibit 9: P/E chart



Source: MOSL, Company

Exhibit 10: P/B chart



Source: MOSL, Company

Financials and Valuations

Consolidated - Income Statement

(INR Million)

| Y/E March | FY14 | FY15 | FY16 | FY17 | FY18E | FY19E | FY20E |
|-------------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Income from Operations | 11,167 | 13,279 | 14,603 | 14,599 | 16,387 | 21,614 | 27,076 |
| Less: Excise Duty | 209 | 350 | 308 | 247 | 353 | 424 | 531 |
| Total Income from Operations | 10,959 | 12,929 | 14,295 | 14,353 | 16,035 | 21,190 | 26,545 |
| Change (%) | 43.4 | 18.0 | 10.6 | 0.4 | 11.7 | 32.2 | 25.3 |
| Total Expenditure | 9,376 | 10,843 | 11,528 | 11,364 | 12,996 | 16,952 | 21,024 |
| % of Sales | 85.6 | 83.9 | 80.6 | 79.2 | 81.1 | 80.0 | 79.2 |
| EBITDA | 1,583 | 2,086 | 2,767 | 2,988 | 3,039 | 4,238 | 5,521 |
| Margin (%) | 14.4 | 16.1 | 19.4 | 20.8 | 19.0 | 20.0 | 20.8 |
| Depreciation | 298 | 527 | 643 | 715 | 762 | 1,319 | 1,582 |
| EBIT | 1,285 | 1,560 | 2,124 | 2,273 | 2,277 | 2,919 | 3,939 |
| Int. and Finance Charges | 204 | 323 | 399 | 323 | 359 | 374 | 396 |
| Other Income | 43 | 43 | 77 | 99 | 140 | 127 | 159 |
| PBT bef. EO Exp. | 1,124 | 1,280 | 1,802 | 2,050 | 2,058 | 2,672 | 3,702 |
| EO Items | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| PBT after EO Exp. | 1,124 | 1,280 | 1,802 | 2,050 | 2,058 | 2,672 | 3,702 |
| Current Tax | 305 | 287 | 535 | 652 | 720 | 908 | 1,259 |
| Deferred Tax | 66 | 83 | 82 | -9 | 0 | 0 | 0 |
| Tax Rate (%) | 33.0 | 29.0 | 34.2 | 31.4 | 35.0 | 34.0 | 34.0 |
| Add: Associate income | 0 | 0 | 0 | 247 | 175 | 250 | 350 |
| Reported PAT | 753 | 909 | 1,185 | 1,654 | 1,513 | 2,013 | 2,793 |
| Adjusted PAT | 753 | 909 | 1,185 | 1,654 | 1,513 | 2,013 | 2,793 |
| Change (%) | 130.8 | 20.8 | 30.3 | 39.6 | -8.5 | 33.1 | 38.7 |
| Margin (%) | 6.9 | 7.0 | 8.3 | 11.5 | 9.4 | 9.5 | 10.5 |

Consolidated - Balance Sheet

(INR Million)

| Y/E March | FY14 | FY15 | FY16 | FY17 | FY18E | FY19E | FY20E |
|-------------------------------------|--------------|--------------|---------------|---------------|---------------|---------------|---------------|
| Equity Share Capital | 203 | 204 | 217 | 229 | 254 | 254 | 254 |
| Total Reserves | 3,357 | 4,107 | 6,444 | 8,807 | 13,611 | 14,945 | 16,744 |
| Net Worth | 3,560 | 4,312 | 6,660 | 9,036 | 13,865 | 15,199 | 16,998 |
| Minority Interest | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Deferred Liabilities | 403 | 549 | 646 | 565 | 565 | 565 | 565 |
| Total Loans | 4,417 | 4,872 | 4,767 | 5,981 | 5,981 | 6,481 | 6,731 |
| Capital Employed | 8,380 | 9,732 | 12,074 | 15,582 | 20,410 | 22,245 | 24,293 |
| Gross Block | 6,539 | 8,438 | 9,622 | 10,099 | 17,599 | 20,099 | 22,099 |
| Less: Accum. Deprn. | 1,714 | 2,272 | 2,941 | 3,656 | 4,417 | 5,737 | 7,319 |
| Net Fixed Assets | 4,825 | 6,166 | 6,681 | 6,443 | 13,182 | 14,362 | 14,780 |
| Goodwill on Consolidation | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Capital WIP | 1,246 | 620 | 766 | 2,605 | 962 | 1,271 | 1,593 |
| Total Investments | 2 | 2 | 2 | 1,082 | 2 | 2 | 2 |
| Curr. Assets, Loans&Adv. | 3,848 | 5,184 | 7,080 | 8,633 | 9,031 | 10,075 | 12,380 |
| Inventory | 1,742 | 2,245 | 3,071 | 2,761 | 3,205 | 4,180 | 5,184 |
| Account Receivables | 1,109 | 1,326 | 1,526 | 4,177 | 4,393 | 5,515 | 6,545 |
| Cash and Bank Balance | 418 | 653 | 1,419 | 498 | 240 | -1,198 | -1,326 |
| Loans and Advances | 580 | 959 | 1,065 | 1,198 | 1,194 | 1,578 | 1,977 |
| Curr. Liability & Prov. | 1,640 | 2,295 | 2,521 | 3,183 | 2,767 | 3,466 | 4,461 |
| Account Payables | 1,355 | 1,887 | 1,791 | 2,160 | 1,602 | 1,858 | 2,304 |
| Other Current Liabilities | 162 | 233 | 608 | 934 | 682 | 901 | 1,129 |
| Provisions | 123 | 175 | 122 | 89 | 483 | 708 | 1,029 |
| Net Current Assets | 2,208 | 2,888 | 4,559 | 5,451 | 6,265 | 6,609 | 7,919 |
| Appl. of Funds | 8,379 | 9,732 | 12,074 | 15,582 | 20,410 | 22,245 | 24,293 |

Financials and Valuations

Ratios

| Y/E March | FY14 | FY15 | FY16 | FY17 | FY18E | FY19E | FY20E |
|-------------------------------|------|------|------|------|-------|-------|-------|
| Basic (INR) | | | | | | | |
| EPS | 3.7 | 4.5 | 5.5 | 7.2 | 6.3 | 7.9 | 11.0 |
| Cash EPS | 5.2 | 7.0 | 8.4 | 10.4 | 9.0 | 13.1 | 17.2 |
| BV/Share | 17.6 | 21.1 | 30.7 | 39.5 | 54.6 | 59.9 | 67.0 |
| DPS | 0.4 | 0.5 | 0.6 | 1.0 | 1.5 | 2.2 | 3.3 |
| Payout (%) | 11.0 | 13.6 | 13.9 | 16.2 | 30.3 | 33.7 | 35.6 |
| Valuation (x) | | | | | | | |
| P/E | 32.1 | 26.7 | 21.8 | 16.5 | 18.8 | 15.0 | 10.8 |
| Cash P/E | 23.0 | 16.9 | 14.1 | 11.5 | 13.3 | 9.1 | 6.9 |
| P/BV | 6.8 | 5.6 | 3.9 | 3.0 | 2.2 | 2.0 | 1.8 |
| EV/Sales | 3.2 | 2.7 | 2.4 | 2.5 | 2.3 | 1.8 | 1.5 |
| EV/EBITDA | 22.0 | 16.8 | 12.4 | 12.2 | 12.1 | 9.1 | 7.1 |
| Dividend Yield (%) | 0.3 | 0.4 | 0.5 | 0.8 | 1.3 | 1.9 | 2.7 |
| Return Ratios (%) | | | | | | | |
| RoE | 23.9 | 23.1 | 21.6 | 21.1 | 13.2 | 13.9 | 17.4 |
| RoCE | 19.8 | 18.7 | 21.4 | 17.9 | 13.9 | 14.7 | 18.1 |
| RoIC | 15.9 | 14.6 | 15.2 | 14.7 | 9.7 | 9.3 | 11.3 |
| Working Capital Ratios | | | | | | | |
| Asset Turnover (x) | 1.3 | 1.3 | 1.2 | 0.9 | 0.8 | 1.0 | 1.1 |
| Inventory (Days) | 58 | 63 | 78 | 70 | 73 | 72 | 71 |
| Debtor (Days) | 36 | 36 | 38 | 104 | 98 | 93 | 88 |
| Creditor (Days) | 77 | 92 | 86 | 116 | 73 | 66 | 66 |
| Leverage Ratio (x) | | | | | | | |
| Current Ratio | 2.3 | 2.3 | 2.8 | 2.7 | 3.3 | 2.9 | 2.8 |
| Interest Cover Ratio | 6 | 5 | 5 | 7 | 6 | 8 | 10 |
| Debt/Equity | 1.2 | 1.1 | 0.7 | 0.7 | 0.4 | 0.4 | 0.4 |

Consolidated - Cash Flow Statement

(INR Million)

| Y/E March | FY14 | FY15 | FY16 | FY17 | FY18E | FY19E | FY20E |
|----------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|
| OP/(Loss) before Tax | 1,124 | 1,280 | 1,801 | 2,050 | 2,058 | 2,672 | 3,702 |
| Depreciation | 298 | 527 | 643 | 715 | 762 | 1,319 | 1,582 |
| Interest & Finance Charges | 190 | 309 | 347 | 278 | 219 | 247 | 237 |
| Direct Taxes Paid | -238 | -317 | -490 | -595 | -720 | -908 | -1,259 |
| (Inc)/Dec in WC | -310 | -363 | -915 | -557 | -910 | -1,579 | -1,184 |
| CF from Operations | 1,064 | 1,435 | 1,387 | 1,891 | 1,409 | 1,751 | 3,078 |
| Others | 16 | 18 | 51 | 43 | -163 | -203 | -254 |
| CF from Operating incl EO | 1,080 | 1,453 | 1,438 | 1,934 | 1,246 | 1,548 | 2,824 |
| (inc)/dec in FA | -2,649 | -1,473 | -1,335 | -3,088 | -5,857 | -2,809 | -2,321 |
| (Pur)/Sale of Investments | 95 | 0 | 0 | 0 | 1,080 | 0 | 0 |
| Others | 8 | 17 | 53 | -90 | 140 | 127 | 159 |
| CF from Investments | -2,546 | -1,456 | -1,281 | -3,178 | -4,636 | -2,682 | -2,162 |
| Issue of Shares | 11 | 11 | 1,059 | 829 | 3,775 | 0 | 0 |
| (Inc)/Dec in Debt | 1,709 | 628 | 191 | 151 | 0 | 500 | 250 |
| Interest Paid | -205 | -319 | -406 | -319 | -359 | -374 | -396 |
| Dividend Paid | -47 | -83 | -234 | -223 | -459 | -679 | -994 |
| Others | 0 | 0 | 0 | 0 | 175 | 250 | 350 |
| CF from Fin. Activity | 1,467 | 238 | 609 | 438 | 3,132 | -303 | -791 |
| Inc/Dec of Cash | 0 | 236 | 766 | -805 | -258 | -1,438 | -128 |
| Opening Balance | 417 | 417 | 653 | 1,303 | 498 | 240 | -1,198 |
| Closing Balance | 417 | 653 | 1,419 | 498 | 240 | -1,198 | -1,326 |

| Explanation of Investment Rating | |
|----------------------------------|--|
| Investment Rating | Expected return (over 12-month) |
| BUY | >=15% |
| SELL | < - 10% |
| NEUTRAL | > - 10% to 15% |
| UNDER REVIEW | Rating may undergo a change |
| NOT RATED | We have forward looking estimates for the stock but we refrain from assigning recommendation |

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Disclosure of Interest Statement

Granules India

Analyst ownership of the stock

No

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