

INDUSTRY	PHARMA		
CMP (as on 24 Jul 2018)	Rs 92		
Target Price	Rs 120		
Nifty	11,134		
Sensex	36,825		
KEY STOCK DATA			
Bloomberg	GRAN IN		
No. of Shares (mn)	254		
MCap (Rs bn) / (\$ mn)	23/338		
6m avg traded value (Rs mn)	290		
STOCK PERFORMANCE (%)			
52 Week high / low	Rs 151/72		
	3M	6M	12M
Absolute (%)	(17.7)	(34.5)	(35.5)
Relative (%)	(24.1)	(36.3)	(49.7)
SHAREHOLDING PATTERN (%)			
Promoters	44.9		
FIs & Local MFs	6.2		
FPIs	9.0		
Public & Others	39.9		
<i>Source : BSE</i>			

Recovery in sight

Continued growth in API and Formulations coupled with the launch of gMethergine led to 20%YoY growth in revenue, coming up to Rs 4.5bn for 1QFY19. The absence of inventory write-off and one-off R&D which were seen last quarter along with improved raw material pricing resulted into a 700bps QoQ jump in EBITDA margin to 16%. Other Income was up 52%QoQ largely driven by forex gain to the tune of Rs 110mn. Also, GRAN earned Rs 147mn (up 351%QoQ) in share of profits from its JVs - Biocause and Omnicem. As a result, reported PAT was at Rs 518mn, up 41%YoY and 153%QoQ.

GRAN commenced sales of gMethergine in June-18 and captured over 50% of the US market share. While this has only affected 1 month in 1QFY19, it looks very promising for GRAN and is expected to add 15-20% to its earnings for the year provided it sustains the current level of market share. Since gMethergine is a fairly complex product, and Teva is the only supplier for its APIs, entry barriers are high.

After a disappointing 4QFY18 performance, GRAN has showed good recovery in profitability in 1QFY19. With 6 ANDA launches in FY19, our thesis of GRAN becoming a US formulation player has started playing out.

Financial Summary

(Rs mn)	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)	FY17E	FY18	FY19E	FY20E
Net Sales	4,532	3,787	19.7	5,038	(10.0)	14,106	16,846	19,034	21,499
EBIDTA	726	769	(5.7)	436	66.4	2,988	2,784	3,335	4,166
APAT	518	368	40.7	204	153.4	1,645	1,329	1,968	2,527
Diluted adj. EPS (Rs)	2.26	1.61	40.7	1.14	99.3	7.5	5.2	7.8	10.0
P/E (x)						12.1	17.4	11.7	9.1
RoE (%)						21.0	12.0	14.3	16.5

Source: Company, HDFC sec Inst Research # Consolidated

However, there are several headwinds for margin improvement (increased revenue R&D and spike in raw material prices), which led to substantial cut in our estimates after 4QFY18 result. However, the share price has also fallen from Rs 140 to Rs 90 since then. At CMP, the stock is trading at 17.4x FY18E, 11.7x FY19E and 9.1x FY20E, still 50% cheaper to industry peers. We continue to maintain BUY with a TP of Rs 120 (12x FY20E).

Highlights of the quarter

- The FDF, API and PFI segments grew 23%, 29% and 0% YoY respectively (1QFY19). The contribution of Ibuprofen revenues was lower at 18% v/s 26% in 4QFY18. Moreover, the emerging market contribution increased to 39% v/s 33% in 1QFY18. Low margin API sales accounted for 40% of revenues, contribution remaining same as the previous quarter.
- Passing previous quarter's increased raw material cost on to the customers was the key reason for revival of gross margin in 1QFY19. Management has guided for 18-19% EBITDA margin in FY19.
- **Near term outlook:** Expect stock to recover post 1QFY19 result on the back of gMethergine market share gain and 5 more ANDA launches in FY19.

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GRAN maintained growth momentum as top line was up 20% YoY

Employee cost increased by 18% sequentially which includes the effect of an employee bonus component. This will normalize over the next quarter, and the revised base would be close to Rs 465mn (up 10%QoQ)

EBITDA margin showed improvement QoQ which can be attributed to (1) passing on previous quarter's increase in cost of materials to customers, (2) absence of the one-off R&D expenditure of Rs 240mn in 4QFY18, (3) increase in contribution of high-margin formulations

Subsequently, PAT margin also showed improvement due to gains in foreign exchange and increase in profits from JVs

Quarterly Financials Snapshot (Consolidated)

Particulars	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)
Net Sales	4,532	3,787	19.7	5,038	(10.0)
Material Expenses	2,471	1,800	37.3	3,097	(20.2)
Employee Expenses	503	390	28.7	424	18.6
Other Expenses	832	828	0.6	1,081	(23.0)
EBITDA	726	769	(5.7)	436	66.4
Depreciation	245	176		204	
EBIT	481	593	(19.0)	232	107.0
Other Income	147	3.8		97	
Interest Cost	65	82		62	
PBT	563	515	9.2	267	110.8
Tax	191	177		95	
Minority Interest	146	30		32	
RPAT	518	368	40.7	204	153.4

Source: Company, HDFC sec Inst Research

Margin Analysis

	1QFY19	1QFY18	YoY (bps)	4QFY18	QoQ (bps)
Material Expenses % Net Sales	54.5	47.5	701	61.5	(695)
Employee Expenses % Net Sales	11.1	10.3	78	8.4	268
Other Expenses % Net Sales	18.4	21.9	(349)	21.5	(308)
EBITDA Margin (%)	16.0	20.3	(430)	8.7	736
Tax Rate (%)	34.0	34.4	(47)	35.6	(163)
RPAT Margin (%)	11.4	9.7	171	4.1	737

Source: Company, HDFC sec Inst Research

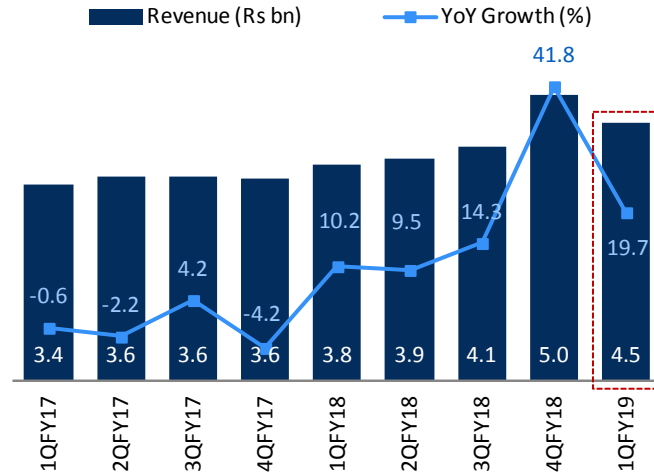
Top-line continued to grow in double digits owing to growth in formulations and API businesses

Formulations continued to expand, and have now grown 23% YoY in 1QFY19. This was largely driven by continued growth in OTC supplies to US partner

Fresh capacities coming on-stream boosted APIs share in the business mix to 40% in 1QFY19

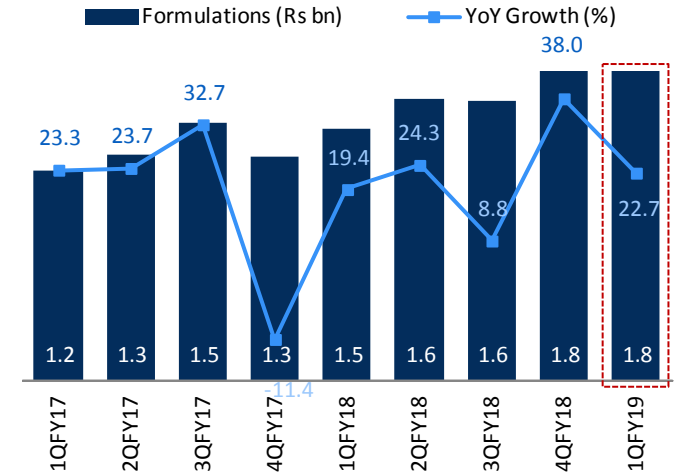
Mgt has guided for a return to 19-20% EBITDA margin in FY19E due to improved gross margins and profits from gMethergine will be realized in H2FY19

Top-line Growth In Double Digits



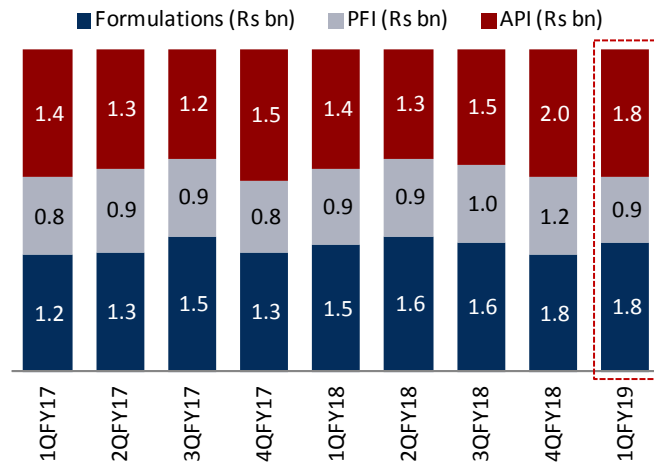
Source: Company, HDFC sec Inst Research

Growth In Formulations Continues



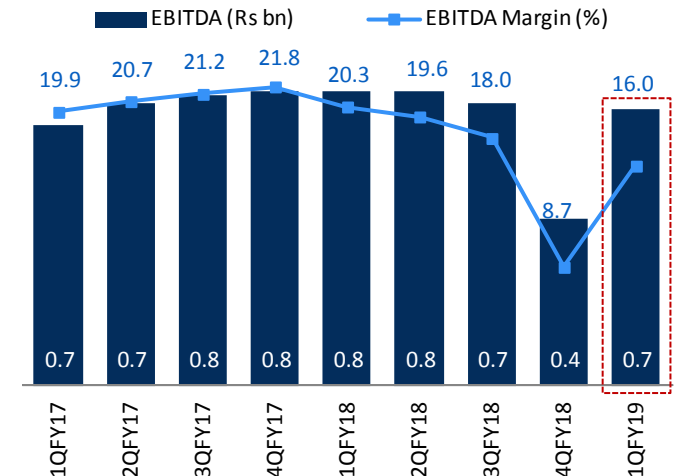
Source: Company, HDFC sec Inst Research

Formulations At Par With API Contribution



Source: Company, HDFC sec Inst Research

EBITDA Margin Recovery



Source: Company, HDFC sec Inst Research

APIs and FDFs continued high growth YoY while PFIs remained flat

Segmental Quarterly Performance

(Rs mn)	1QFY19	1QFY18	YoY (%)	4QFY18	QoQ (%)
Segmental Revenues					
Finished Dosages	1,813	1,477	22.7	1,814	(0.0)
PFIs	906	909	(0.3)	1,209	(25.0)
APIs	1,813	1,401	29.4	2,015	(10.0)

Source: HDFC sec Inst Research

Assumptions

	FY16	FY17	FY18	FY19E	FY20E
Finished Dosages	4,417	5,388	6,582	7,570	8,705
<i>Growth (%)</i>	7.0	22.0	22.2	15.0	15.0
PFIs	3,843	3,401	4,046	4,532	5,075
<i>Growth (%)</i>	24.0	(11.5)	19.0	12.0	12.0
APIs	5,737	5,380	6,230	6,933	7,718
<i>Growth (%)</i>	0.6	18.6	15.8	11.3	11.3
Total	13,997	14,169	16,858	19,034	21,499
<i>Growth (%)</i>	8.3	1.2	19.0	12.9	12.9

Source: HDFC sec Inst Research

Peer Set Comparison

	Mcap (Rs bn)	CMP (Rs/sh)	Reco	TP/FV	Adj EPS (Rs/sh)				P/E (x)				RoE (%)			
					FY17	FY18	FY19E	FY20E	FY17	FY18	FY19E	FY20E	FY17	FY18	FY19E	FY20E
Sun Pharma	1,354	563	BUY	640	26.0	13.0	16.4	24.6	21.7	43.4	34.2	22.9	17.9	9.1	12.3	14.8
Cipla	504	627	NEU	565	12.5	17.5	23.2	30.0	50.2	35.8	27.1	20.9	8.4	10.5	12.4	14.2
Cadila Healthcare	382	372	BUY	525	14.5	12.9	14.6	21.2	25.6	29.0	25.5	17.6	23.5	16.8	16.1	20.1
Lupin	369	821	BUY	1,200	33.4	38.0	39.6	59.7	24.6	21.6	20.7	13.7	12.2	12.7	12.5	16.8
Dr Reddy's Labs	352	2,076	NEU	2,340	72.7	59.2	75.7	102.5	28.6	35.1	27.4	20.3	9.5	7.8	9.5	11.5
Aurobindo Pharma	348	594	BUY	740	39.3	34.4	39.0	48.0	15.1	17.3	15.2	12.4	27.6	19.1	17.9	18.6
Divi's Labs	287	1,080	NEU	1,095	39.9	33.0	44.6	51.4	27.0	32.7	24.2	21.0	22.0	15.5	18.7	18.9
Torrent Pharma	248	1,465	BUY	1,590	51.2	40.1	52.4	72.0	28.6	36.6	28.0	20.4	22.1	15.1	17.9	21.1
Alkem Laboratories	242	2,026	BUY	2,445	74.6	57.6	76.8	101.9	27.2	35.2	26.4	19.9	21.9	14.8	17.6	20.1
Glenmark	159	563	BUY	710	29.6	17.5	27.0	38.8	19.0	32.2	20.8	14.5	18.1	9.4	12.8	16.1
Jubilant Life Sciences	119	762	BUY	1,060	37.0	46.6	65.5	80.4	20.6	16.3	11.6	9.5	18.0	19.3	22.4	22.5
Alembic Pharma	104	553	NEU	535	21.4	21.9	22.1	29.7	25.9	25.3	25.1	18.6	23.0	20.0	17.5	20.4
Laurus Labs	48	451	NR	505	18.0	15.8	17.9	28.0	25.1	28.5	25.2	16.1	17.4	11.9	12.0	15.9
Dishman Carbogen Amcis	43	267	BUY	450	9.0	9.6	13.6	19.9	29.7	27.9	19.7	13.5	3.0	3.1	4.2	5.9
Strides Shasun	33	365	NEU	420	34.0	12.7	18.4	26.3	10.7	28.7	19.8	13.9	13.1	4.4	6.5	8.7
Suven Life Sciences	30	238	NR	450	6.8	9.7	10.3	11.4	34.8	24.5	23.1	20.9	13.8	17.2	16.0	15.5
Granules India	23	92	BUY	120	7.5	5.2	7.8	10.0	12.2	17.5	11.8	9.2	21.0	12.0	14.3	16.5
Neuland Labs	5	615	BUY	1,000	42.6	11.0	28.9	62.3	14.4	56.1	21.3	9.9	12.8	2.2	5.5	11.1

Source: HDFC sec Inst Research

Change In Estimates (Consolidated)

Rs mn	Previous			New			Change (%)		
	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E
Revenue	16,846	19,034	21,499	16,846	19,034	21,499	0.0	0.0	0.0
EBITDA	2,784	3,335	4,166	2,784	3,335	4,166	0.0	0.0	0.0
APAT	1,329	1,801	2,428	1,329	1,968	2,527	0.0	9.3	4.1

Source: HDFC sec Inst Research

Income Statement (Consolidated)

Year ending March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Net Revenues	13,572	14,106	16,846	19,034	21,499
Growth (%)	5.0	3.9	19.4	13.0	12.9
Material Expenses	7,250	6,796	8,963	9,803	10,857
Employee Expenses	1,176	1,402	1,652	1,961	1,999
Other Expenses	2,383	2,919	3,447	3,936	4,476
EBITDA	2,763	2,988	2,784	3,335	4,166
EBITDA Margin (%)	20.4	21.2	16.5	17.5	19.4
EBITDA Growth (%)	32.4	8.2	(6.8)	19.8	24.9
Depreciation	584	715	762	1,002	1,124
EBIT	2,179	2,273	2,022	2,333	3,042
Other Income (Including EO Items)	52	99	108	286	107
Interest	371	323	331	379	365
PBT	1,860	2,050	1,800	2,239	2,784
Tax (Incl Deferred)	611	652	634	672	807
Minority Interest / Share of profit	19	247	160	400	550
RPAT	1,268	1,645	1,326	1,968	2,527
EO (Loss) / Profit (Net Of Tax)	-	-	-	-	-
APAT	1,268	1,645	1,329	1,968	2,527
APAT Growth (%)	39.4	29.8	(19.2)	48.0	28.4
Adjusted EPS (Rs)	6.1	7.5	5.2	7.8	10.0

Source: Company, HDFC sec Inst Research

Balance Sheet (Consolidated)

Year ending March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
SOURCES OF FUNDS					
Share Capital - Equity	217	229	254	254	254
Reserves	6,399	8,807	12,788	14,269	15,809
Total Shareholders Funds	6,616	9,036	13,042	14,523	16,063
Long Term Debt	1,842	1,242	4,457	3,832	6,482
Short Term Debt	3,929	4,738	5,125	5,550	2,400
Total Debt	5,771	5,981	9,582	9,382	8,882
Net Deferred Taxes	479	541	474	474	474
Other Non-current Liabilities & Provns	47	39	24	60	897
TOTAL SOURCES OF FUNDS	12,912	15,596	23,121	24,469	26,346
APPLICATION OF FUNDS					
Net Block	5,599	6,443	10,012	11,510	11,636
CWIP	766	2,605	2,901	2,500	2,500
Investments	701	1,082	1,566	1,250	1,250
Other Non-current Assets	295	259	359	320	320
Total Non-current Assets	7,361	10,390	14,837	15,580	15,706
Cash & Equivalents	1,303	498	1,156	883	2,807
Inventories	2,537	2,760	2,799	3,441	3,799
Debtors	3,753	4,177	6,171	6,258	6,479
Other Current Assets	586	915	1,406	1,588	1,794
Total Current Assets	6,877	7,852	10,376	11,287	12,072
Creditors	1,811	2,160	2,522	3,011	3,324
Other Current Liabilities & Provns	817	984	726	270	915
Total Current Liabilities	2,628	3,144	3,248	3,281	4,239
Net Current Assets	4,249	4,708	7,128	8,006	7,833
TOTAL APPLICATION OF FUNDS	12,912	15,596	23,121	24,469	26,346

Source: Company, HDFC sec Inst Research

Cash Flow

Year ending March (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Reported PBT	1,860	2,050	1,800	2,239	2,784
Non-operating & EO items	716	-	-	-	-
Interest expenses	318	223	222	94	258
Depreciation	584	715	762	1,002	1,124
Working Capital Change	(735)	(467)	(2,435)	(842)	1,010
Tax Paid	(611)	(652)	(634)	(672)	(807)
OPERATING CASH FLOW (a)	2,132	1,869	(284)	1,821	4,369
Capex	(1,509)	(3,658)	(4,626)	(2,099)	(1,250)
Free cash flow (FCF)	623	(1,789)	(4,910)	(278)	3,119
Non-operating Income	86	(250)	(375)	601	107
INVESTING CASH FLOW (b)	(1,423)	(3,908)	(5,001)	(1,498)	(1,218)
Debt Issuance/(Repaid)	30	210	3,602	(200)	(500)
Interest Expenses	(371)	(323)	(331)	(379)	(365)
FCFE	368	(2,152)	(2,014)	(256)	2,286
Share Capital Issuance	805	1,345	2,977	-	-
Dividend	(169)	(246)	(334)	(486)	(987)
Others	(249)	247	169	330	550
FINANCING CASH FLOW (c)	47	1,234	6,082	(735)	(1,303)
NET CASH FLOW (a+b+c)	756	(806)	797	(412)	1,848
Closing Cash & Equivalents	1,304	497	1,295	744	2,732

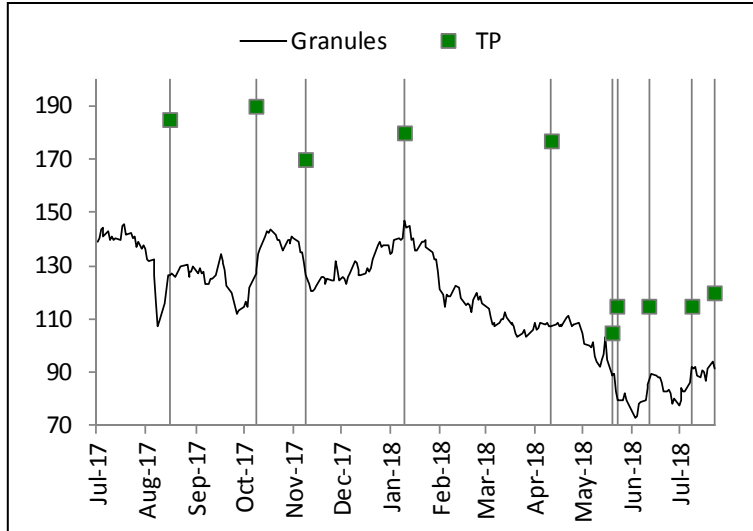
Source: Company, HDFC sec Inst Research

Key Ratios

	FY16	FY17	FY18	FY19E	FY20E
PROFITABILITY (%)					
GPM	46.6	51.8	46.8	48.5	49.5
EBITDA Margin	20.4	21.2	16.5	17.5	19.4
APAT Margin	9.3	11.7	7.9	10.3	11.8
RoE	23.2	21.0	12.0	14.3	16.5
RoIC (or Core RoCE)	14.8	12.7	7.8	7.8	9.8
RoCE	13.0	13.1	8.0	9.4	11.0
EFFICIENCY					
Tax Rate (%)	32.9	31.8	35.2	30.0	29.0
Fixed Asset Turnover (x)	1.6	1.4	1.2	1.1	1.2
Inventory (days)	68.2	71.4	60.7	66.0	64.5
Debtors (days)	100.9	108.1	133.7	120.0	110.0
Other Current Assets (days)	15.8	23.7	30.5	30.5	30.5
Payables (days)	48.7	55.9	54.6	57.7	56.4
Other Current Liab & Provns (days)	22.0	25.5	15.7	5.2	15.5
Cash Conversion Cycle (days)	114.3	121.8	154.4	153.5	133.0
Debt/EBITDA (x)	2.1	2.0	3.4	2.8	2.1
Net D/E (x)	0.7	0.6	0.6	0.6	0.4
Interest Coverage (x)	5.9	7.0	6.1	6.2	8.3
PER SHARE DATA (Rs)					
EPS	6.1	7.5	5.2	7.8	10.0
Dividend	0.6	0.8	1.1	1.6	3.3
Book Value	26.1	35.6	51.4	57.2	63.3
VALUATION					
P/E (x)	13.4	10.9	15.7	10.6	8.2
P/BV (x)	3.1	2.3	1.6	1.4	1.3
EV/EBITDA (x)	8.0	8.1	10.5	8.8	6.5
EV/Revenues (x)	1.6	1.7	1.7	1.5	1.3
OCF/EV (%)	9.6	7.7	(1.0)	6.2	16.2
FCF/EV (%)	2.8	(7.4)	(16.8)	(0.9)	11.6
FCFE/Mkt Cap (%)	2.1	(11.5)	(9.7)	(1.2)	11.0
Dividend Yield (%)	0.7	1.0	1.3	2.0	4.0

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
17-Aug-17	127	BUY	185
10-Oct-17	126	BUY	190
11-Nov-17	127	BUY	170
11-Jan-18	147	BUY	180
13-Apr-18	107	BUY	177
21-May-18	95	NEU	105
25-May-18	83	BUY	115
13-Jun-18	85	BUY	115
10-Jul-18	86	BUY	115
25-Jul-18	92	BUY	120

Rating Definitions

- BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
- NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
- SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

INSTITUTIONAL RESEARCH

Disclosure:

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