

## Pharmaceutical – 1QFY16 Results Review

### Green shoots – Recovery in US generics, India back on growth track

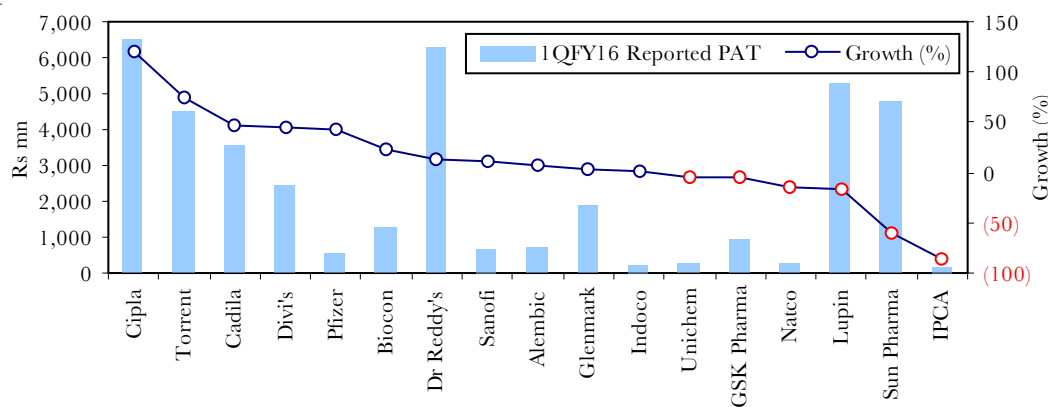
Our universe's revenues and profit growth in 1QFY16 were in line with our expectations as aggregate revenues grew by 11.7% YoY to Rs 283 bn (B&Kc: Rs 286 bn) and PAT declined by 2% to Rs 40 bn (B&Kc: Rs 46 bn, 6% growth). Adjusted PAT came in line at Rs 45 bn, 7% growth. However, our coverage universe actually displayed improvement of 60 bps in EBITDA margin to 26.7% (against our expectation of 310 bps dip) due to companies like Torrent Pharma, Cipla, Cadila and Dr Reddy's Labs showing better than expected growth in the US market.

### Key takeaways from 1QFY16 – USFDA approvals to lead recovery

- We believe that the US generics market will start seeing some traction from 2QFY16 as there has been an uptick in the approval rate from the USFDA for few Indian companies like Glenmark, Aurobindo, Alembic and Lupin. US region grew by 10% YoY to US\$ 1.4 bn in 1QFY16.
- Stringent compliance standards from USFDA resulted in delayed approval for many products but has also improved pricing scenario for certain players (Abilify and Nexium). Channel consolidation is resulting in weeding out non-competent players which would further improve scenario in market.
- India's annual growth is coming back to the level similar to three years ago (12-14%). Domestic players are seeing good volume uptick. Aggregate domestic revenues grew by 11% YoY to Rs 88 bn.
- In Emerging Markets, currency headwinds in Russia, Venezuela and Brazil remain a cause of concern – key affected players include Dr Reddy's, Glenmark, Ipca and Torrent.
- Pharma companies are increasing their R&D expenses with increased filings in niche therapy areas/novel products. Average R&D spend was ~8.3% of net sales in 1Q to Rs 20 bn (US\$ 313 mn).

**Top picks** – Increased compliance from USFDA will push companies to improve their quality standards. This would benefit companies in the long-run, move up the value chain and make strategic M&A moves to consolidate their position. With currency tailwinds in support, we recommend Sun Pharma, Divi's, Dr Reddy's, Cadila and Sanofi.

### PAT growth for B&K Universe

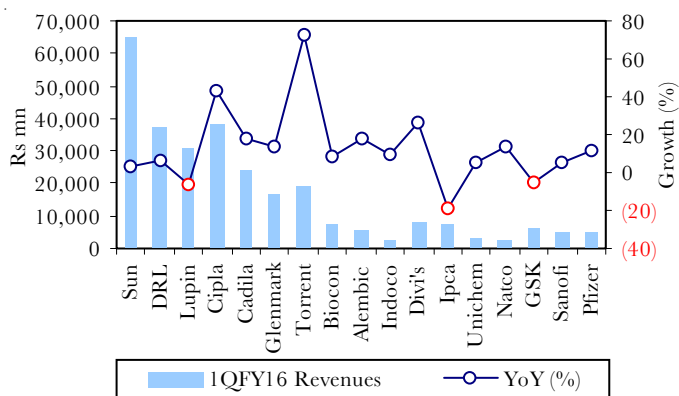


Source: B&K Research

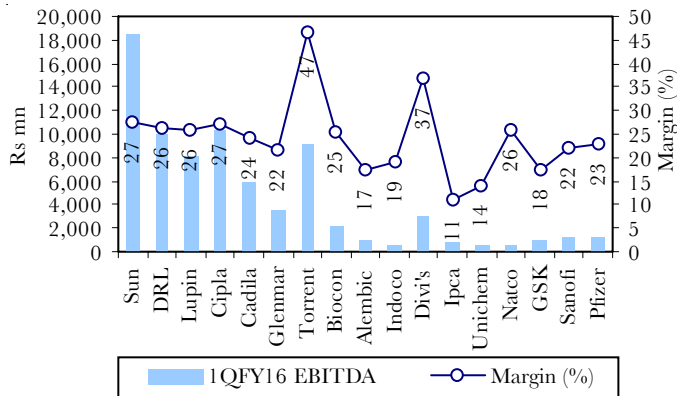
## B&amp;K Universe – Company’s highlights and remarks for 1QFY16

(Rs mn)	Revenues		Reported PAT		Adjusted PAT		EBITDA mgn (%)		Remarks
	1QFY16	YoY (%)	1QFY16	YoY (%)	1QFY16	YoY (%)	1QFY15	1QFY16	
Sun Pharma	65,222	3.3	4,790	(60.2)	9,928	(29.6)	30.6	27.4	Margin recovery a positive largely driven by Taro. Resolution of Halol unit is critical for growth (no ANDA approval since September 2014).
Dr Reddy’s	37,578	6.8	6,257	13.7	6,186	20.6	25.1	26.4	UCB business got consolidated this quarter (10 days of sales). US business remained healthy. Currency worries in Russia, CIS and Venezuela.
Lupin	30,743	(6.4)	5,250	(16.0)	5,250	(16.0)	33.4	25.9	Performance impacted due to competition in Suprax and high base effect of gCymbalta.
Cipla	37,768	42.7	6,506	120.9	6,506	120.9	19.9	27.0	Strong performance led by Esomeprazole supplies to Teva. Base business growth also remains healthy.
Cadila	23,783	17.7	3,534	47.1	3,391	43.6	18.3	24.1	Sustained performance in US drives growth. Improvement in pace of approvals to boost earnings.
Glenmark	16,424	13.4	1,910	3.3	1,910	18.6	21.4	21.7	Sees sustained approvals of products in the US. Domestic business remains strong.
Torrent	18,860	72.7	4,490	75.4	4,490	94.3	31.0	46.7	Windfall gains on account of Aripiprazole launch in the US. Elder portfolio driving domestic business. Brazil facing currency headwinds.
Biocon	7,598	8.6	1,262	22.7	1,262	22.7	24.0	25.5	Profitability mostly driven by Syngene as well as one-time gain due to capacity reservation fee. Approval of Malaysian facility remains key to growth for insulin sales.
Alembic	5,824	18.0	699	8.1	699	8.1	19.4	17.5	Aripiprazole profits to reflect in 2QFY16 (one quarter lag). Limited competition.
Indoco	2,160	9.1	203	1.1	203	1.1	18.4	19.1	Restructuring of business divisions in India impacts performance. Change in Ophthalmic alliance partner (from Allergan to Teva). Ramp-up critical for earnings.
Divi’s	8,069	26.1	2,432	44.8	2,262	35.6	36.6	37.1	Performance boost due to supplies from DSN SEZ Unit II.
Ipca Labs	7,510	(19.1)	189	(86.2)	280	(79.7)	24.7	10.8	Exports hampered due to currency fluctuations and absence of institutional business. Domestic growth is weak. No clarity on resolution of import alerts.
Unichem	3,048	5.6	288	(4.7)	266	(11.9)	15.0	13.8	Domestic growth recovering. Sustainability would be the key trigger for re-rating.
Natco	2,157	13.2	282	(15.6)	282	(15.6)	27.2	25.7	Sofosbuvir growing well in India. Copaxone approval remains the key event in the near term.
GSK Pharma	6,219	(5.1)	933	(5.1)	949	(3.5)	17.3	17.5	Supply constraints continued to impact performance. Resolution underway.
Sanofi	5,143	5.7	642	11.7	642	11.7	19.4	22.1	Improvement in margin driven by cost rationalisation. To benefit from price increases and volume share gains in the coming quarters.
Pfizer	4,792	11.2	538	43.4	538	43.4	22.9	23.1	Key brands continue to perform well. Exhibited strongest growth in our MNC universe in 1QFY16.
<b>Total</b>	<b>282,896</b>	<b>11.7</b>	<b>40,204</b>	<b>(2.1)</b>	<b>45,044</b>	<b>6.7</b>	<b>26.1</b>	<b>26.7</b>	

### Revenue growth was subdued at 12% YoY

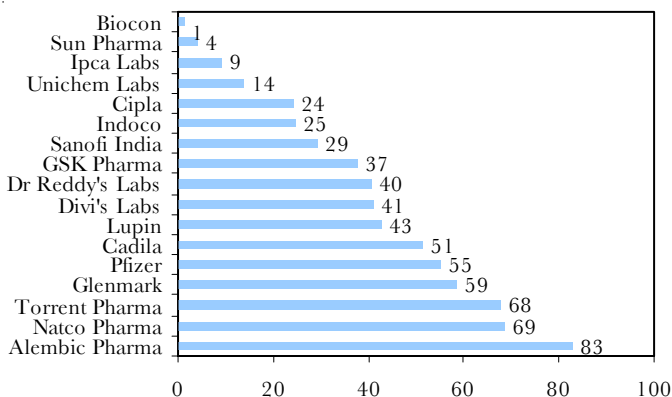


### Margin remains at healthy levels for majority of the companies (average of 27%)

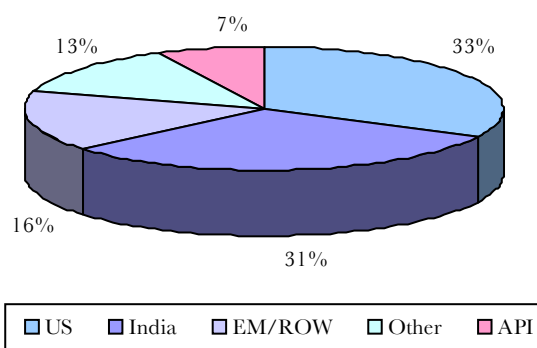


Source: B&K Research

### 52-week performance (%)

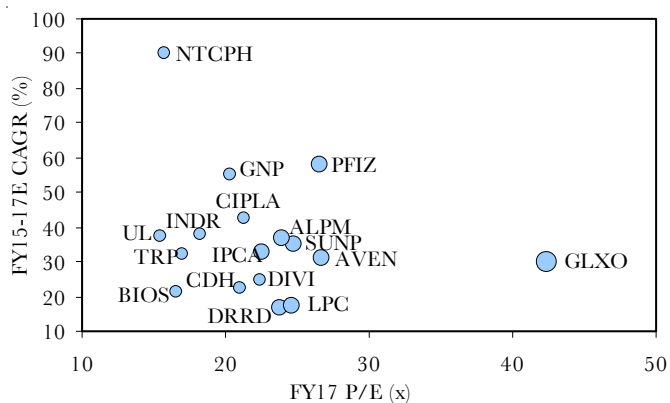


### 1QFY16 geography break-up for B&K Universe

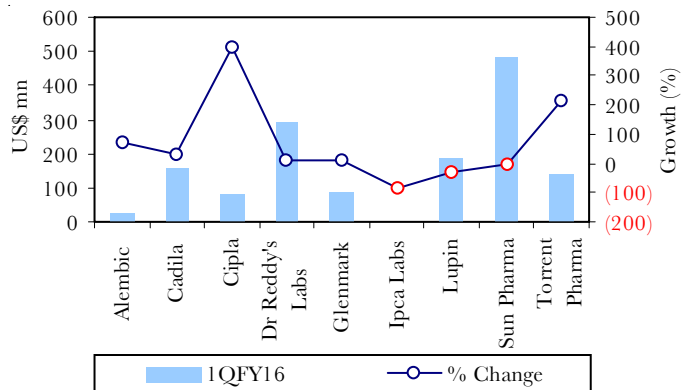


Source: B&K Research

### FY15-17E CAGR versus P/E



### Revenue growth in US



Source: B&K Research

## US Generics – Best market to expand operations

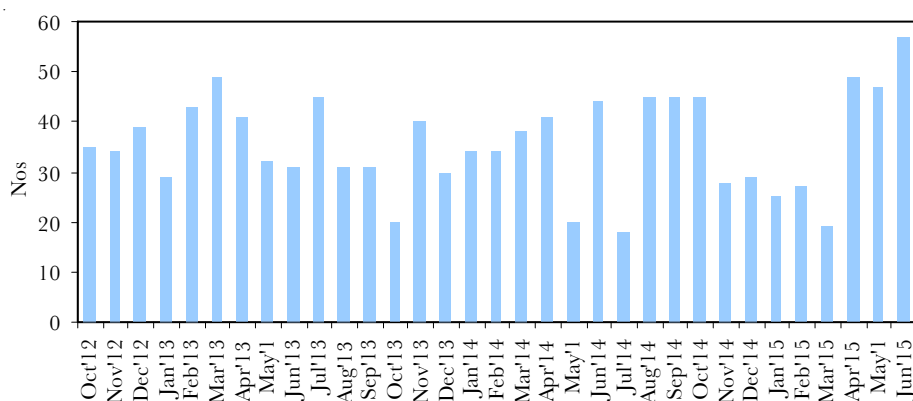
The US generics market remains a prime driver of earnings for Indian pharma companies as demand for generic drugs continue to be robust led by patent expiry of key drugs (US\$ 75 bn worth set to expire over the next two-three years) and increasing pressure on US healthcare system to expand population coverage under Obamacare. While patent expiries in US are ongoing event, an interesting trend which is emerging is the lack of competitive pressure for few drugs like Abilify and Nexium which are leading to extraordinary results for those players who have approvals in place viz. Torrent and Alembic (for Abilify), Cipla (for gNexium supply to Teva). This situation has arisen on account of FDA issues at several Indian company sites due to which approvals have been delayed.

Reasons for lack of approvals vary from non-compliance to cGMP standards, Quality control issues, incidence of product recalls in US market, data integrity problems unearthed during FDA inspections, etc. which have resulted in not many players being fully compliant and has led to a general slowdown in pace of approvals. As a result, there have been several incidence of increase in generic drug prices in the US as there are drug shortages in the market (especially for injectables) and increasing cost of compliance as FDA standards have become quite stringent and still evolving. These problems are not limited to Indian generic companies but are happening on global scale (also seen in US, China, Europe, etc.)

### Key issues facing Indian pharma sector

- 1). Slowdown in approvals.
- 2). USFDA compliance related matters leading to delays in approval timeline.
- 3). Consolidation (among generic players as well channel distributors).
- 4). Price increases – driven by drug shortages (Taro, Dr Reddy's, Cadila).
- 5). Reduced competition as approvals are held back, Nexium and Abilify are two examples of good opportunities due to FDA related issues.
- 6). Increasing focus on Novel and Complex generics – emerging trend.

### Monthly ANDA approval trend



Source: CDER

### Mixed performance in June 2015 quarter – lack of FDA approvals has affected growth

Our universe saw a healthy growth of 16% in INR terms to Rs 92 bn for the US market on YoY basis, also helped by the currency tailwinds of ~6%. In dollar terms, US growth was

subdued at 10% to US\$ 1.4 bn. Share of US region to overall revenues remains healthy at 33% with highest contribution coming from Sun which derives nearly 50% of its revenues (share has come down from 60% including Ranbaxy).

### US performance in 1QFY16

Company	1QFY16 (Rs mn)	% growth	% of total sales	Comments
Alembic Pharma	1,425	78.9	24	Growth on account sales booked on account of limited competition in the gAbilify, related profits will however be shown in 2QFY16.
Cadila Healthcare	9,850	37.5	41	Low base and price hikes in specific products like HCQS resulted in strong growth for Cadila.
Cipla	5,161	429.7	14	Sales of Eesomeprazole supply to Teva in 4QFY15 where Teva filled channel inventory were reported in 1QFY16 (~US\$ 60 mn).
Dr Reddy's Labs	18,515	14.3	49	Improved product mix resulted in better than expected sales and profitability.
Glenmark Pharmaceuticals	5,610	14.8	34	Received 6 approvals during the quarter but most of the growth for the US to follow in consecutive quarters.
Ipca Labs	80	(86.0)	1	Import alert continues to affect US sales. Exempted products are struggling to gain market share.
Lupin	11,906	(25.8)	39	High base due to gCymbalta and generic competition for Suprax has affected the US sales. Acquired GAVIS to drive US sales.
Sun Pharmaceuticals	30,906	2.2	47	Supply constraints due to ongoing Halol resolution affected the US sales but Taro continues to show strong performance. Ex-Taro sales up by US\$ 30 mn aided by sustained performance of DUSA and URL.
Torrent Pharmaceuticals	8,880	230.1	47	Limited competition in gAbility domain brings windfall gains for Torrent which was better than expected (~US\$ 120 mn).
<b>Total</b>	<b>92,333</b>	<b>16.0</b>	<b>33</b>	

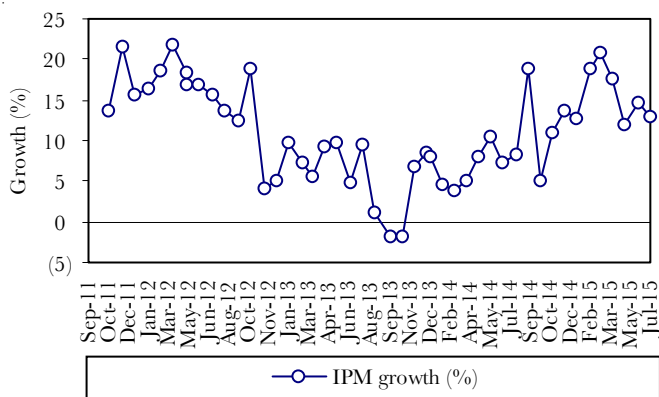
**B&K's view** – After facing headwinds of slow approval rate (33 months on average) and channel consolidation related price pressures in the US generic market, there are some signs of recovery for Indian companies. The uptick in the rate of approval for companies like Glenmark, Aurobindo, Alembic and Lupin indicate FDA's commitment to clear backlog of ANDAs. The pricing pressure on account of channel consolidation has formed a base and the incremental impact would diminish in the following quarters. Most of the managements indicated towards capitalising on the USFDA approvals (secured in 1QFY16) from 2QFY16 which should see some improvements. We expect our universe to demonstrate growth of 22% in the US generics for FY16 & sustain at that pace in future. Maintaining the status quo in the limited competition opportunities like gAbilify, early approvals for key drugs like Nexium, Gleevec and resolution of pending USFDA related issues (Halol for Sun Pharma, Srikakulam for Dr Reddy's, Moraiya for Cadila and all facilities of Ipca) can provide further upsides to our estimates and would drive valuations further. We remain positive on the overall growth in the US generics segment.

### Domestic market – Recovery underway, NLEM extension could be a dampener

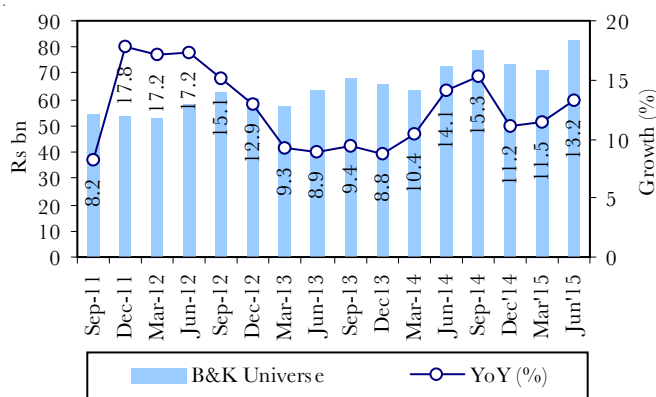
This is the second largest segment for Indian pharma companies (31% of total revenue in 1QFY16) after US and is quite an important piece as most players are quite well entrenched in their respective therapy areas and domestic branded business throws up quite a decent chunk of cash flows. While gross margins for few players have been affected (more for MNC's) by NLEM price reduction policy of 2013, most of the players are on the recovery mode which can be seen in improved growth rates posted by player in June 2015 quarter. Our covered universe displayed growth of 11.3% YoY in 1QFY16 for the domestic formulation business. The growth was mainly led by the Indian pharma companies which grew by 13.2% while MNC pack grew at a tepid rate of 2.5%.

As per the IMS June 2015 MAT, Indian pharma market grew by 13.8% to Rs 943 bn. This was the highest MAT growth achieved by the IPM in a span of three years indicating that IPM is now again back on the strong growth track. Indian pharma companies posted a strong growth of 15% while the pharma MNC pack grew by 10% during the same period. The issues related to price adjustment on account of DPCO 2013 and slow growth of the economy is behind us and companies are slowly able to garner volume growth and are also working on price hikes wherever possible.

#### Growth is improving



#### Domestic sales growth (B&K Universe)



Source: B&K Research

Amongst the Indian companies, Alembic (17% YoY), DRL (19% YoY), Glenmark (19%), Lupin (16%) and Torrent Pharma (39%) were able to grow above average. Increasing share of chronic therapy sales for Alembic, Glenmark and Lupin is resulting in strong growth. New product launches and prescription growth allowed DRL to show strong growth while better than expected performance from erstwhile Elder portfolio is driving Torrent's sales. Amongst the MNC pack, Pfizer reported very good sales growth of 11% YoY since most of its key brands (Prevenar, Becosules, Gelusil) have been performing well. Sanofi sales though grew by 6%, were in line with expectations but the profitability improved significantly (EBITDA margin 22%, up 270 bps). Supply constraints impacted GSK Pharma's sales which declined by 5% during the quarter.

Although the recovery is seen in the domestic sales growth, a possible expansion of NLEM list would be a negative development to watch for.

## Key triggers for companies

Company	Key triggers	Remarks
Alembic Pharma	5 approvals since April 2015 (including Abilify). Front end presence in the US likely by 4QFY16E.	Continues to benefit from limited competition in Abilify. More product launches to result in strong growth in the US business.
Biocon	Commercialisation of the Malaysia facility, Syngene listing (Mkt. cap of US\$ 1.05 bn).	Biocon would be able to start supplying insulin to the emerging markets thus supporting higher growth for biopharma segment.
Cadila Healthcare	Resolution of Moraiya manufacturing facility is critical.	Close to 165 ANDA's are pending and improvement in pace of approvals post resolution would boost earnings.
Cipla	Exclusive supplies of Nexium for US market (competition emerging from Mylan approval). Launch of Salmeterol/Fluticasone MDI in UK (approval pending).	Nexium earnings likely to taper off. Salmeterol/fluticasone MDI has the biggest market of US\$ 400 mn in UK among European countries. Would bring windfall profit for Cipla.
Divi's Laboratories	New unit DSN SEZ II to witness higher utilisation. Capex plans of Rs 5 bn at Kakinada for a greenfield unit by FY17-18.	To drive 20-25% CAGR in revenues for FY16-17E.
Dr Reddy's Labs	Resolution of Srikakulam API facility (Nexium approval), Devaluation of Venezuelan Bolivar.	Would enable the approval of gNexium which can lift earnings by 10-12% for FY16-17E. Venezuela revenue ~US\$ 134 mn (6% of revenue). Further devaluation of Bolivar can impact near term earnings.
Glenmark Pharmaceuticals	7 approvals on YTD basis. Devaluation of Bolivar. Near term launch of Welchol, Seasonique and Zetia in FY17. Vatelizumab NCE in Phase II – licenced to Sanofi.	65 ANDA's pending. As all plants are compliant, we expect timely approval. Vatelizumab progress to expand valuations. Venezuela exposure is <5% of revenue.
Indoco Remedies	Supply of ophthalmic products to US.	Alliance with Allergan/Actavis to get transferred to Teva which has acquired US rights.
Ipca Labs	Resolution of Pithampur (Formulations) and Ratlam (API) manufacturing facilities, resuming institutional anti-malarial supply.	USFDA re-inspection of the facilities is pivotal but no clear timeline available, institutional business to be normal from 3QFY16.
Lupin	Higher rate of approvals for both Lupin and GAVIS. Possible resolution of Form 483 observations at Goa plant (Nexium).	Lupin's pipeline has expanded to over 160 ANDA's following GAVIS acquisition for US\$ 880 mn.
Natco Pharma	Approval of gCopaxone remains key trigger while any positive development in the litigation of gRevlimid would secure Natco's position as exclusive generic.	gCopaxone and gRevlimid remains one of the most important drugs with NPV of Rs 154 and Rs 401, respectively.
Sun Pharmaceuticals	FDA resolution of Halol unit. Positive news from Tildrakizumab phase III trials. Taro's NDA approval for Keveyis smooth integration of Ranbaxy.	All pending approvals like Abilify, Gleevec, SPARC's Xelpros likely to get cleared. Manufacturing rationalisation and product transfer to Sun's facilities to benefit in the medium to long-term.
Torrent Pharmaceuticals	Higher competition in the gAbilify space. Currency headwinds in the Brazilian market.	Profitability and cash flow would be dependent on gAbilify competitive scenario.
Unichem Labs	Turnaround in domestic growth. Higher approvals for the US.	US approvals pending for quite some time. Waiting time > 48 months. Sustained performance in domestic business likely to lead to further re-rating of the stock.
GlaxoSmithKline Pharma	Expansion of NLEM, supply constraints.	Resolution of supply constraints to boost margin and performance. Majority of NLEM impact has been absorbed. To benefit from price increases and volume share gains. Expansion of NLEM list may not have any significant negative impact.
Sanofi India	Expansion of NLEM, price increases.	Earnings to improve on the back of price increases and volume share gains for its portfolio. Inclusion of combinations in the essential list of medicines can dent near term earnings.
Pfizer	Expansion of NLEM, growth in Prevenar vaccine, Price increases.	17% of current sales are under price control. Expansion of NLEM list can have negative effect though the erstwhile Wyeth portfolio may be less affected.

## Emerging markets/Rest of the World – Currency headwinds

In 2014, emerging markets (Asia and Latin America) reported sales of US\$ 277 bn contributing 26% to the global sales. Asian market have grown at a CAGR of 12.4% for the last three years to attain size of US\$ 202 bn while Latin American market grew by 10.2% CAGR in the same period to US\$ 76 bn. IMS expects the Asian pharma market to post a CAGR of 7-10% till 2019 while the Latin American market is expected to grow at 5-8% in the same period.

Indian companies have been prudently expanding their presence in the emerging markets for years sensing the growth potential as well as the ease of operations and it's similarity to Indian branded generic market. The profitability in some of these markets also remains high compared to India and the regulatory network is less stringent.

EM/RoW sales for the companies under our coverage grew by 14% during 1QFY16. Most of the emerging markets are facing fluctuations of the currency and hence, it is becoming little unpredictable at the current juncture to forecast sales. However, most of the Indian companies are consolidating their presence in the emerging markets considering the overall growth potential it has to offer. We expect our coverage universe to post a growth 13% collectively for emerging markets in FY16.

Cipla saw the maximum growth amongst the peers in the emerging markets since it is now benefitting from the consolidation drive it had initiated in FY15. It has been establishing front ends in the key markets like Yemen, Sri Lanka, Uganda, etc. MedPro in South Africa is also performing well due to participation in tenders for therapeutic areas other than the traditional areas like anti-AIDS and anti-infective. Its partnership with Teva in SA for distribution of the products is performing well. DRL (31% YoY), Indoco Remedies (23% YoY) and Lupin (24% YoY) also put up a good show in the emerging markets.

Alembic Pharma (64% YoY down) and Ipca Labs (51% YoY down) saw major decline for the emerging markets. Adverse currency movements have affected business of both the companies in the emerging markets. Sun (7% down) may continue to post subdued results for EMs due to integration of Ranbaxy and defocusing the non-core business.

Devaluation of the Venezuelan Bolivar remains one of the biggest concerns especially for DRL and Glenmark. In Venezuela, DRL recorded sales of US\$ 135 mn (5% of total sales) while Glenmark reported US\$ 45 mn (4% of total sales), in FY15.

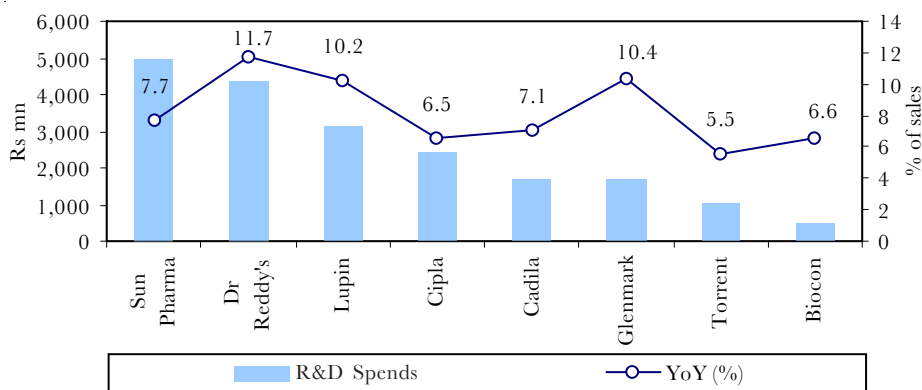
## R&D spend on the uptick, now at 8.3% of revenues

This is a significant driver of valuations for Indian companies as they continue to spend significantly on R&D projects which indicates their strategic intent to expand further and deeper into key markets of US, India and EM's. Overall R&D spend was at Rs 20 bn (US\$ 313 mn) which was up by 34% YoY and now accounts for 8.3% of revenues.

Though overall ANDA filings have been maintained around similar rate historically (barring Cadila which is targeting to file around 40 ANDA's in FY16), the quality of filings have gone up for major players with major focus on building a pipeline around novel and complex technologies, niche areas like Derma, Oncology, Ophthalmics, etc. Innovative players like SPARC and Dr Reddy's have started filing for NDA applications for their novel drugs (innovative formulations based on drug delivery technologies). Injectables remains a key



### R&D spends remain on the higher end



Source: B&K Research

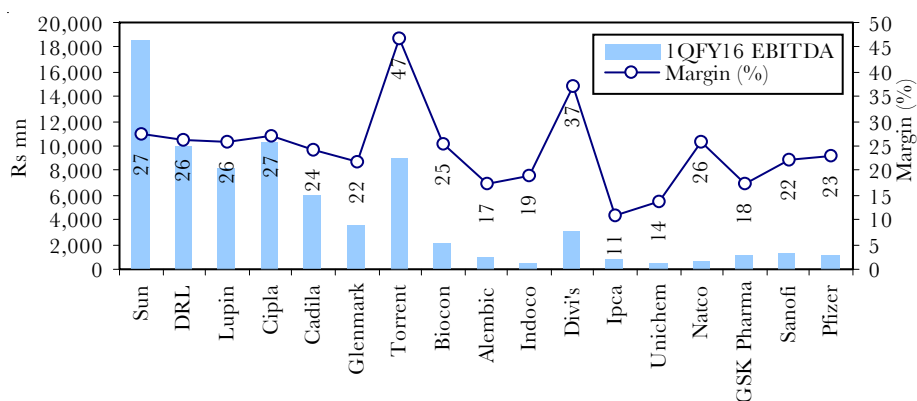
priority area for most players as there are tremendous drug shortages in Injectables space owing to highly stringent standards followed by USFDA for sterile units.

### EBITDA margins still on an upswing...

Despite higher R&D spends by Indian companies, EBITDA margins on an aggregate basis have still gone up (better than our expectations) as few players like Torrent and Cipla have shown exemplary performance in the US region on back of key launches (Abilify and Nexium, respectively). Overall EBITDA margins were up 60 bps to 26.7%. While Torrent saw margins going up by 1,570 bps to 46.7%, Cipla's margins expanded by 710 bps to 27%. Material costs on aggregate basis increased by just 6% to Rs 93 bn on account of better product mix and inventory rationalisation. Lupin and GSK Pharma saw reduction of 11% and 12%, respectively, while Torrent and Divi's witnessed an increase of 40% and 29%, respectively, owing to uptick of certain products and increase in capacity utilisation rates. Aggregate employee costs increased by 12% to Rs 47 bn. Majority of the increase has been on account of annual salary increases and addition and rationalisation of manpower in select therapies/geographies.

Majority of the increase in other expenses can largely be attributable to higher R&D spends for building future pipeline and increased compliance costs for players facing regulatory issues.

### Margin remains at healthy levels



Source: B&K Research

### Aggregate P&L for B&K Universe

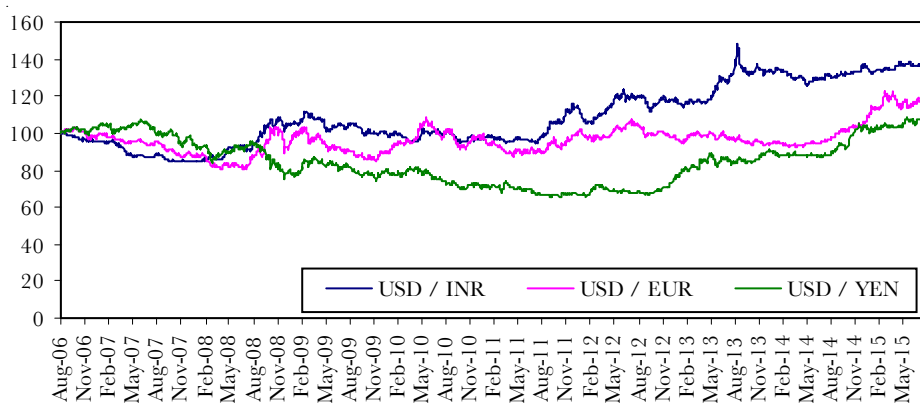
(Rs mn)	1QFY15	1QFY16	YoY (%)
Revenues	253,334	282,896	11.7
Material cost	88,225	93,393	5.9
Employee cost	42,359	47,325	11.7
R&D expenses	15,164	20,437	34.8
Other expenses	60,830	73,720	21.2
EBITDA	67,013	77,517	15.7
EBITDA margin (%)	26.1	26.7	–
PAT	41,047	40,204	(2.1)
Adjusted PAT	42,201	45,044	6.7

### Currency related impact – positive for exporters

With rupee depreciating further to levels of Rs 66, we feel that Indian exporters would further benefit, especially for those players who have indigenous production (local costs). Divi's is a key gainer as it derives nearly 87% of its revenues from exports and 80% of the export revenues is dollar denominated. Other companies which have net exports share at 60% plus revenues include Cadila Healthcare, Dr Reddy's Laboratories, Glenmark Pharmaceuticals, Lupin, Natco Pharma and Sun Pharmaceuticals. US remains one of the major revenue contributors for majority of the companies, however, these companies also have exposure to markets like Europe, Venezuela, Latin America and EMs. Hence the benefit would partially get negated due to adverse currency movements in these regions. In Venezuela, USDVEF stands at 600 (unofficial) as against SIMADI USDVEF rate of 193 and CENCOEX USDVEF rate of 6.3. The net impact would still be positive for most of the companies.

Companies who have raised forex debt would have to provide for MTM losses on their books (either in P&L or in Balance Sheet). Here, companies which could be vulnerable include Sun Pharmaceuticals (on account of Ranbaxy's debt), Aurobindo, Ipca Labs, Glenmark, etc.

### Movement of various currencies against USD



Source: B&K Research

## Impact of INR depreciation against USD

Company (Rs mn)	FY15				Net exports as % of revenues	Debt in forex	Impact of INR depreciation against USD – Positive
	Gross revenue	Exports	Imports*	Net exports			
Alembic Pharma	20,330	8,590	2,234	6,356	31.3	438	To benefit from increasing exposure to US markets (~80-85% of regulated markets business).
Biocon	22,416	10,993	5,853	5,140	22.9	10,918	No major impact.
Cadila	86,577	56,335	3,768	52,567	60.7	7,891	US is 65% of exports, however, benefit may partially get negated due to adverse currency movement in LatAm and EMs and forex debt.
Cipla	111,264	62,325		62,325	56.0	8,438	No major impact.
Divi's Labs	30,639	26,568	7,250	19,317	63.0	–	Positive impact as 80% of the exports revenues is dollar denominated. Biggest beneficiary.
Dr Reddy's Labs	148,189	127,031	9,488	117,543	79.3	40,698	To gain from US exposure (~50% of revenue) but would partially get negated due to adverse currency movement in Russia, CIS and Venezuela.
Glenmark Pharma	66,149	48,659	NA	NA	NA	28,500	US is largest market for Glenmark but lower benefits due to adverse currency movement Venezuela and other EMs, exposure to forex debt.
Ipca Labs	30,599	17,529	3,755	13,774	45.0	7,500	No major impact as US business has been impacted due to import alert on its facilities.
Lupin	127,700	93,851	7,963	85,888	67.3	1,461	To gain from US exposure but benefit are negated due to adverse currency movement in Emerging Markets and South Africa.
Natco Pharma	8,466	5,936	NA	NA	NA	5,250	Net impact of the rupee depreciation is positive as Natco also has presence in US retail segment.
Sun Pharma	275,708	208,543	NA	NA	NA	40,000	To aid overall growth (US ~50% of revenue), however, impact may remain soft on account of lower uptick in revenues from Halol, legacy Ranbaxy forex debt.
Torrent Pharma	46,530	30,440	2,444	27,996	60.2	–	Higher revenue from the US due to gAbilify would help margins but the Brazilian currency depreciation will keep check on it.
Sanofi India**	19,230	4,977	7,298	(2,321)	(12.1)	–	Imports likely to get costlier.
GSK Pharma**	33,786	63	4,334	(4,271)	(12.6)	–	Imports likely to get costlier.

\*Raw material + Stores and spares consumed.

\*\*Imports for the year are on CIF basis as reported by the company.

## Change in actuals versus estimates

(Rs mn)	Revenues			EBITDA			Adjusted PAT		
	1QFY16	1QFY16E	Var. (%)	1QFY16	1QFY16E	Var. (%)	1QFY16	1QFY16E	Var. (%)
Cipla	37,768	31,881	18.5	10,390	7,426	39.9	6,506	4,350	49.6
Unichem	3,048	2,776	9.8	427	298	43.2	266	186	42.8
Torrent	18,860	14,264	32.2	9,090	5,396	68.5	4,490	3,556	26.3
Divi's	8,069	7,357	9.7	2,999	2,745	9.2	2,262	1,959	15.5
Biocon	7,598	8,188	(7.2)	2,122	1,960	8.3	1,262	1,133	11.4
Dr Reddy's	37,578	38,777	(3.1)	9,941	9,089	9.4	6,186	5,745	7.7
Cadila	23,783	23,406	1.6	6,015	4,914	22.4	3,391	3,292	3.0
Sanofi	5,143	5,135	0.2	1,214	1,061	14.4	642	655	(2.0)
Pfizer	4,792	4,605	4.1	1,118	1,049	6.5	538	618	(12.9)
Glenmark	16,424	16,944	(3.1)	3,596	4,153	(13.4)	1,910	2,193	(12.9)
Sun Pharma	65,222	69,179	(5.7)	18,497	18,971	(2.5)	9,928	12,016	(17.4)
Lupin	30,743	37,173	(17.3)	8,166	10,360	(21.2)	5,250	6,759	(22.3)
Indoco	2,160	2,286	(5.5)	426	463	(7.9)	203	261	(22.4)
GSK Pharma	6,219	6,943	(10.4)	1,100	1,464	(24.8)	949	1,246	(23.9)
Natco	2,157	2,331	(7.5)	575	670	(14.2)	282	410	(31.1)
Alembic	5,824	6,401	(9.0)	1,021	1,547	(34.0)	699	1,088	(35.8)
IPCA	7,510	8,354	(10.1)	822	1,219	(32.6)	280	540	(48.1)
<b>Total</b>	<b>282,896</b>	<b>286,000</b>	<b>(1.1)</b>	<b>77,517</b>	<b>72,784</b>	<b>6.5</b>	<b>45,044</b>	<b>46,007</b>	<b>(2.1)</b>

## Change in full year estimates

(Rs mn)	Old		Revised		Change (%)		Rating change	Remarks
	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E		
<b>Sun Pharmaceuticals</b>								
Revenues	278,941	334,069	291,691	345,387	4.6	3.4	Maintain BUY	Revision in assumptions is on account of higher other operating income received during 1QFY16 on divestment of brands as mandated by the regulatory authorities (CCI, US FTC) and expected reduction in one-charges in the coming quarters. Our estimates include Gleevec sales of US\$ 64 mn and US\$ 220 mn in FY16E and FY17E, respectively. Complete resolution of Halol and smooth integration of Ranbaxy continue to remain the key trigger for driving future growth.
EBITDA	77,766	118,689	87,747	122,325	12.8	3.1		
PAT	50,046	84,119	55,459	86,777	10.8	3.2		
EPS (Rs)	20.8	35.0	23.0	36.1	10.8	3.1		
<b>Lupin</b>								
Revenues	147,630	178,158	145,654	172,267	(1.3)	(3.3)	Maintain OP	US business growth revised downward on account of negative impact of channel consolidation resulting in 4% impact on FY16 earnings. Addition of Gavis would benefit and provide immediate boost to US revenues once the transaction is closed.
EBITDA	42,152	51,590	41,124	50,079	(2.4)	(2.9)		
PAT	27,909	34,387	26,881	33,004	(3.7)	(4.0)		
EPS (Rs)	62.1	76.5	59.8	73.4	(3.7)	(4.0)		
<b>Cipla</b>								
Revenues	133,321	159,050	133,531	159,184	0.2	0.1	Maintain OP	Higher sales from Eesomeprezole supplies leads to 13% increase in FY16 earnings. Key triggers for Cipla would be to commercialise gSeretide in UK and smooth integration of its recent M&As in EMs and RoW markets to derive benefit in future.
EBITDA	28,898	36,666	30,892	38,431	6.9	4.8		
PAT	17,096	22,525	18,546	23,996	8.5	6.5		
EPS (Rs)	21.3	28.1	23.1	29.9	8.5	6.5		
<b>Alembic Pharma</b>								
Revenues	26,999	31,232	28,891	32,539	7.0	4.2	Maintain OP	Upgrade in FY16 estimates is largely on account of Aripiprazole (Abilify) which continues to remain a limited competition opportunity. We expect Abilfy to add US\$ 72 mn to Alembic sales (US\$ 143 mn including the partner). Launch of Para IV and FTF opportunities and commercialisation of its front end in the US would help sustain growth in future.
EBITDA	5,723	7,033	6,987	7,300	22.1	3.8		
PAT	4,050	5,002	5,042	5,299	24.5	5.9		
EPS (Rs)	21.5	26.5	26.7	28.1	24.5	5.9		

(Rs mn)	Old		Revised		Change (%)		Rating change	Remarks
	FY16E	FY17E	FY16E	FY17E	FY16E	FY17E		
<b>Unichem Laboratories</b>								
Revenues	13,123	14,763	13,415	15,064	2.2	2.0	Maintain UP	Recovery in domestic growth is positive, however, sustainability remains crucial for re-rating in future. US business growth has suffered on account of delay in approvals for its ANDAs (Average approval timeline up to 50 months). Improvement in pace of approvals would further boost its performance in future.
EBITDA	1,541	2,092	1,680	2,179	9.0	4.2		
PAT	991	1,400	1,064	1,426	7.4	1.9		
EPS (Rs)	10.9	15.4	11.7	15.7	7.4	1.9		
<b>Natco Pharma</b>								
Revenues	14,579	18,481	12,183	17,245	(16.4)	(6.7)	Maintain OP	Cut in estimates is largely on account of uncertainty over Copaxone approval as well as Sandoz gaining market share and currency headwinds in emerging markets. Domestic business is expected to remain healthy on the back of Hepcinat (Sofosbuvir) sales.
EBITDA	6,457	7,851	4,468	6,273	(30.8)	(20.1)		
PAT	4,449	5,503	2,941	4,283	(33.9)	(22.2)		
EPS (Rs)	134.5	166.4	88.9	129.5	(33.9)	(22.2)		
<b>Torrent Pharmaceuticals</b>								
Revenues	67,546	67,749	69,200	68,744	2.4	1.5	Maintain OP	Better than expected revenues from Abilify leads to 3% upgrade in our EPS for FY16E. Key near term trigger remains approval for Nexium which can lead to further re-rating of future earnings.
EBITDA	21,000	19,176	21,598	19,239	2.8	0.3		
PAT	14,735	12,953	15,196	13,133	3.1	1.4		
EPS (Rs)	87.1	76.6	89.8	77.6	3.1	1.4		

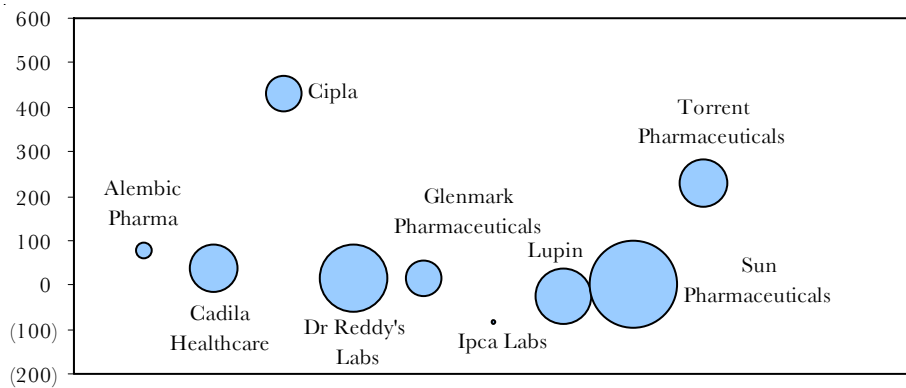
**Note:** OP – Outperformer, UP – Underperformer.

## US pipeline

Company	DMF's	Cumulative ANDA filings	ANDAs approved	Pending*	Para - IV	FY15 US revenues (US\$ mn)	Remarks – Key product triggers
Aurobindo	196	379	174	205	–	595	Focus on injectables (80-85 ANDA's) and complex generics.
Alembic	72	68	38	30	12	58	Among early generic for Abilify. Focus on complex generics. 40% of the filings fall in the Para IV category.
Natco		34	10		14	16	Copaxone and Revlimid launch to improve earnings and cash flows.
Indoco	11	29	8	21	4	12	Focus on ophthalmic products. Also working on 505 (b)(2) and super generic products.
Cadila	116	266	101	165	–	539	Working on transdermals, nasals, topical, injectable, Oncology, NDDS and biogenerics.
Cipla	177	147	79	68	–	140	Follows partnership model with US generic companies (20 partners in the US). In process for setting up its own front end by FY16E. Rumours of bid for Kremers unit in the US.
Dr Reddy's Lab	219	225	152	73	47	1,027	Investing 11-12% in R&D. Building strong pipeline for future. Focus on injectables, biosimilars and other complex products. Pending ANDAs include 16 likely FTFs
Glenmark	72	165	100	65	28	324	Settled on Zetia for December 2015 launch. Building Specialty pipeline for the US.
Jubilant	73	72	38	34		–	Supplying products through Hollistier and Draxis, its US subsidiaries.
Lupin	157	306	142	164	40	866	Acquisition of Gavis boosted its pipeline for US (66 pending + 65 under development).
Sun + Ranbaxy	396	597	438	159	30	2,178	Largest Indian player in the US. Strong presence across various therapies. Gilead settlement – launch in February 2016. Resolution of Halol critical for improving performance.
Torrent	26	73	48	25	–	132	Late entrant into US, building pipeline. Benefiting in low competition products.
Strides + Shasun	66	34	17	17	1	17	Sterile business Agila sold to Mylan for US\$ 1.75 bn, Merger with Shasun makes it an integrated player. Focus remains on US. 100+ products under development.
Wockhardt	71	158	89	73	–	173	Awaiting USFDA resolution for Waluj and Chikalthana units (import alert).
<b>Aggregate</b>	<b>1,652</b>	<b>2,553</b>	<b>1,434</b>	<b>1,099</b>	<b>172</b>	<b>6,076</b>	<b>Indian companies pipeline improving, reducing gap with Teva no.1 player in generics.</b>

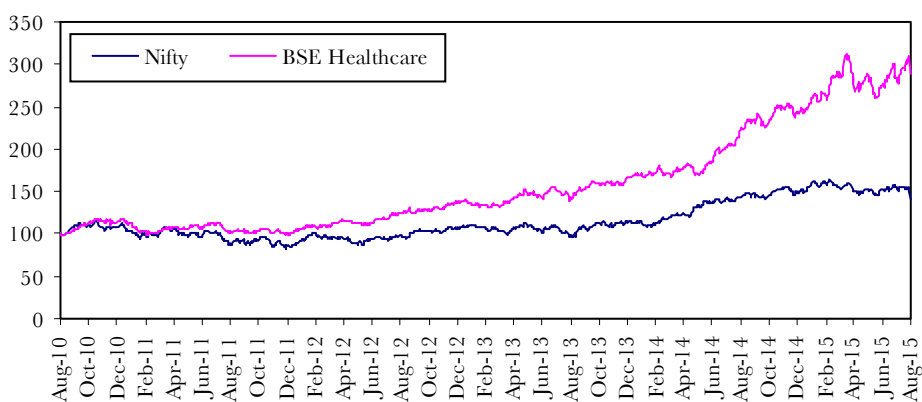
\*Including tentative approvals.

US Revenue versus Growth



Source: B&K Research

Nifty versus BSE Healthcare performance



Source: B&K Research

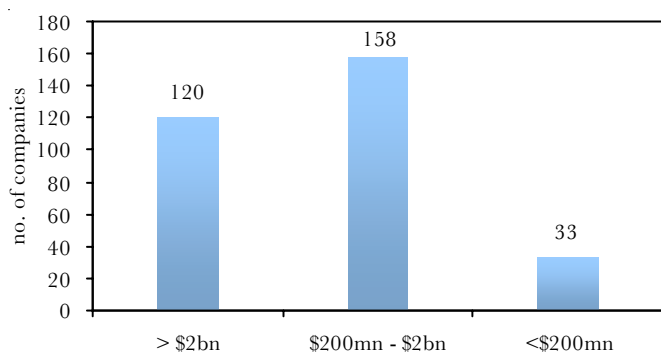


## Valuation

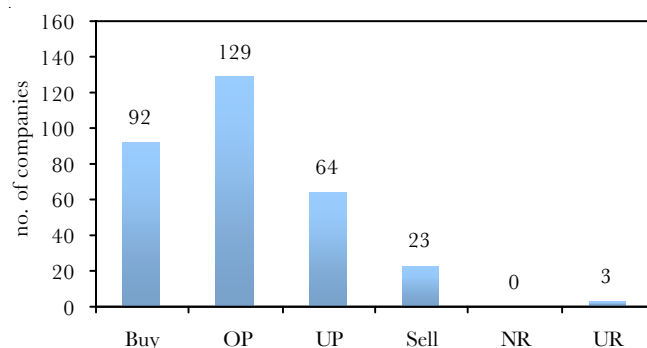
Company	No. of shares (mn)	CMP (Rs)	Target price (Rs)	6m daily avg. vol. (US\$ mn)	Mkt Cap (US\$ mn)	EPS (Rs)			FY15-17E CAGR (%)	P/E (x)		FY15		FY16E	
						FY15	FY16E	FY17E		FY16E	FY17E	RoE (%)	RoCE (%)	EV/ EBITDA (x)	EV/ Sales (x)
<b>Top picks</b>															
Sun Pharma	2,406	891	975	91.1	32.1	19.7	23.0	36.1	35.2	38.7	24.7	21.1	22.4	23.9	7.2
Divi's Labs	133	2,225	2,450	5.0	4.4	64.0	80.9	99.7	24.8	27.5	22.3	26.3	31.8	20.0	7.6
<b>Other Buys</b>															
Dr Reddy's Labs	170	4,043	4,250	18.4	10.3	125.0	145.9	170.3	16.7	27.7	23.7	21.1	19.4	17.4	4.3
Glenmark Pharma	282	1,124	1,150	15.2	4.6	23.0	34.2	55.4	55.0	32.9	20.3	19.3	16.0	19.0	4.1
Sanofi India	23	3,910	4,500	0.8	1.3	85.6	118.5	147.0	31.0	33.0	26.6	14.0	20.6	18.7	4.0
Pfizer	46	2,177	2,475	0.8	1.5	32.8	62.9	82.2	58.2	34.6	26.5	11.4	23.8	18.4	4.3
<b>Outperformer</b>															
Alembic Pharma	189	672	750	2.3	1.9	15.0	26.7	28.1	36.9	25.1	23.9	36.3	35.9	18.0	4.3
Biocon	200	478	525	5.8	1.5	19.6	23.7	28.8	21.3	20.2	16.6	12.5	10.8	11.6	2.7
Cadila	205	1,843	1,930	4.4	5.7	58.4	70.5	88.0	22.7	26.1	20.9	31.1	22.6	17.2	3.8
Cipla	803	636	660	19.4	7.7	14.7	23.1	29.9	42.5	27.5	21.3	11.3	14.6	16.6	3.8
Indoco Remedies	92	313	405	0.4	0.4	9.0	12.7	17.2	38.3	24.6	18.2	17.0	18.9	14.3	2.9
Lupin	450	1,804	1,850	45.6	12.2	53.5	59.8	73.4	17.2	30.2	24.6	30.4	38.5	20.5	5.8
Natco Pharma	33	2,027	2,650	5.4	1.0	35.9	88.9	129.5	90.0	22.8	15.6	15.2	17.5	14.9	5.5
Torrent Pharma	169	1,320	1,370	2.8	3.5	44.2	89.8	77.6	32.4	14.7	17.0	34.1	25.4	10.8	3.4
GSK Pharma	85	3,409	3,650	0.8	4.3	47.7	65.1	80.6	29.9	52.3	42.3	16.7	29.1	40.3	9.8
<b>Underperformer</b>															
Ipsca Labs	126	798	710	3.3	1.5	20.1	23.4	35.5	32.8	34.1	22.5	12.4	14.5	17.6	3.1
Unichem Labs	91	243	235	0.4	0.3	8.3	11.7	15.7	37.5	20.7	15.4	9.0	8.6	13.0	1.6

## B&amp;K Universe Profile

## By Market Cap (US\$ mn)



## By Recommendation



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<b>BUY</b>	>+20% (absolute returns)	>+25% (absolute returns)	>+30% (absolute returns)
<b>OUTPERFORMER</b>	+10% to +20%	+15% to +25%	+20% to +30%
<b>UNDERPERFORMER</b>	+10% to -10%	+15% to -15%	+20% to -20%
<b>SELL</b>	<-10% (absolute returns)	<-15% (absolute returns)	<-20% (absolute returns)

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