

Strides Shasun ----- Maintain OUTPERFORM

Strong outlook driven by Lovaza and Renvela supplies in the near term

EPS: ▼ TP: ▼

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- 1Q FY18 was weak with EBITDA margins at 10.5%, but we stay positive as the near-term outlook is strong on: (1) Lovaza and first modified release approval expected in the near term and market share gains in own products; (2) Sevelamer's supply to partners began in 2Q FY18; (3) clear facilities; & (4) API demerger.
- Strides guided for formulations' business top line to grow at least 20% in FY18 with approvals from the US expected to pick up and Australia growth in low double digits. This should help margins.
- Key disappointment was 21% QoQ fall in regulated business. US hit due to (1) pricing pressure on partnered portfolio; (2) inventory filling in 4Q FY17; and (3) seasonality. However, Strides did well and gained share on its own front-end sales (up QoQ). We cut estimates 32%/15% and TP to Rs1,000 to factor in weak results.
- Other takeaways: (1) ANDA filing momentum is strong (five in FY18 and a target of 15-20 filings in FY18); (2) API demerger has been approved by CCI and stock exchanges; key step is NCLT approval; (3) Malaria supplies were negligible in this quarter and will pick up over the next couple of quarters (rebidding in Sep).

QoQ due to: (1) pricing pressure in the US; (2) inferior mix—higher ARV and lower malaria tender sales; and (3) a currency hit.

Strong outlook; Lovaza and first modified release approval expected in near term

Strides guided for formulations' business top line to grow at least 20% in FY18 with approvals from the US expected to pick up and Australia growth in low double digits. Lovaza and the first modified release approval expected in the near term and Strides has gained market share in own launches in the US. This should help margins. The supply of Sevelamer to partners began in 2Q FY18 and should help the API business.

Strong filing momentum; clean FDA status to help approvals

ANDA filing momentum is strong (five filings in FY18 and a target of 15-20 in FY18). Strides has 29 pending ANDAs in the US. Of these, 16 are plain orals (tablets + hard capsules), while there are seven derma and three modified release products. Strides is one of the few companies that has stayed clean of FDA issues.

Bbg/RIC	STR IN / STSA.BO	Price (11 Aug 17, Rs)	875.20		
Rating (prev. rating)	O (O)	TP (prev. TP Rs)	1,000 (1,185)		
52-wk range (Rs)	1207.9 - 875.2	Est. pot. % chg. to TP	14		
Mkt cap (Rs/US\$ mn)	78,324.3/ 1,221.2	Blue sky scenario (Rs)	1,400		
ADTO-6M (US\$ mn)	4.9	Grey sky scenario (Rs)	650.00		
Free float (%)	65.6	Performance	1M	3M	12M
Major shareholders	Promoter- 34.4%	Absolute (%)	(16.2)	(15.7)	(23.0)
		Relative (%)	(13.6)	(18.7)	(33.9)
Year	03/15A	03/16A	03/17E	03/18E	03/19E
Revenue (Rs mn)	11,958	31,649	36,457	38,072	44,985
EBITDA (Rs mn)	2,289	5,558	6,424	6,547	8,949
Net profit (Rs mn)	1,033	2,458	3,850	2,914	4,958
EPS (CS adj. Rs)	17.3	29.6	43.1	32.6	55.5
- Change from prev. EPS (%)	n.a.	n.a.	0	(32.0)	(15.4)
- Consensus EPS (Rs)	n.a.	n.a.	89.6	47.9	65.7
EPS growth (%)	33.5	70.8	45.5	(24.3)	70.1
P/E (x)	50.5	29.5	20.3	26.8	15.8
Dividend yield (%)	0	0.4	0.6	0.4	0.7
EV/EBITDA (x)	35.0	17.6	15.5	15.1	10.8
P/B (x)	4.6	2.5	2.9	2.6	2.3
ROE (%)	9.6	12.3	13.8	10.3	15.6
Net debt(cash)/equity (%)	15.8	66.4	74.9	67.7	51.9

Note 1: Strides is a mid-sized pharma company, with diversified presence across the US, India, Africa, Australia and other developed markets.

[Click here](#) for detailed financials

Figure 1: Weak regulated market sales; EMs helped by ARV tender

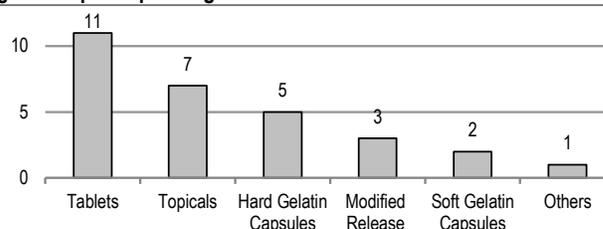
	1Q18A	1Q18E	Diff (%)	1Q17A	Y/Y %	4Q17A	Q/Q %
Regulated Markets	4,147	4,869	-15%	3,706	12%	5,266	-21%
Emerging Markets	2,697	2,147	26%	2,526	7%	2,100	28%
API	1,514	1,526	-1%	1,369	11%	1,517	0%

Source: Company data, Credit Suisse estimates.

Disappointing results due to US pricing hit, weak sales mix

Strides reported weak results as regulated sales declined 21% QoQ and margins fell to 10.4%. The US was hit due to (1) pricing pressure on the partnered portfolio; (2) inventory filling in 4Q FY17; and (3) seasonality. Australia was hit due to stocking issues before the PBS impact takes place. Gross margins declined sharply by 650 bp

Figure 2: Split of pending ANDAs



Source: Company data, Credit Suisse estimates.

Earnings call takeaways:

- API demerger has been approved by CCI and stock exchanges; key step is NCLT approval.
- Malaria supplies were negligible in this quarter and will pick-up over the next couple of quarters (rebidding in Sep)

Figure 3: Strides 1QFY18: weak results

(Rs mn)	1Q18A	1Q18E	Diff (%)	1Q17A	Y/Y %	4Q17A	Q/Q %
Net sales	8,418	8,542	-1%	7,895	7%	8,884	-5%
Gross profit	50%	57%	-7%	53%	-3%	57%	-7%
Personnel cost	17%	18%	-1%	16%	1%	17%	0%
R&D	4%	4%	1%	3%	2%	4%	1%
Other expenses	18%	16%	2%	17%	1%	18%	0%
Total expenditure	7,545	6,961	8%	6,573	15%	7,315	3%
EBITDA	873	1,582	-45%	1,323	-34%	1,569	-44%
EBITDA margin	10.4%	18.5%		16.8%	-6%	17.7%	-7%
Depreciation	511	520	-2%	424	21%	529	-3%
EBIT	362	1,062	-66%	899	-60%	1,040	-65%
Other income	361	325	11%	208	74%	731	-51%
Interest cost	640	540	19%	559	14%	592	8%
Pre-tax income	82	846	-90%	547	-85%	1,179	-93%
Income taxes	-33	144	-123%	88	-138%	175	-119%
Net income	116	702	-84%	459	-75%	1,004	-88%
Minority interest	83	60		65		189	
Net income	6	642	-99%	333	-98%	1,123	-100%

Source: Company data, Credit Suisse estimates.

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Companies Mentioned (Price as of 11-Aug-2017)

Strides Shasun Limited (STSA.BO, Rs875.2, OUTPERFORM, TP Rs1000.0)

Disclosure Appendix

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3-Year Price and Rating History for Strides Shasun Limited (STSA.BO)

STSA.BO Date	Closing Price (Rs)	Target Price (Rs)	Rating
10-Dec-15	1378.05	1720.00	O *
08-Feb-16	1107.30	1515.00	
17-May-16	1160.45	1420.00	
17-Aug-16	1059.05	1235.00	
06-Feb-17	1190.55	1370.00	
18-May-17	1025.90	1185.00	

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Valuation Methodology and Risks: (12 months) for Strides Shasun Limited (STSA.BO)

Method: Our target price of Rs 1000 for Strides is based on 18x FY19E earnings per share (10% discount to peers). Strides is in the process of integrating the acquisitions and current margins are not reflective of the core business. We have an Outperform as we expect margins and ROCE to improve.

Risk: Risks to our target price of Rs1000 and Outperform rating for Strides Shasun Limited include: (1) higher-than-expected impact of PBS cuts, (2) integration issues w.r.t acquisition, (3) adverse currency movements.

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