

## Aurobindo Pharmaceuticals

### Another Feather in the Cap

**Aurobindo Pharmaceuticals (APL)** has acquired dermatology and oral solids businesses from Sandoz Inc., USA for an upfront purchase price of US\$0.9bn in cash. With this acquisition, Aurobindo adds sales of US\$0.9bn and would become the 2<sup>nd</sup> largest generic player in the US by number of prescriptions. Acquisition is funded by debt and values the acquired company at 1.0xEV/sales, which we believe given the size and scope of the business acquired is very attractive. The transaction will lead to net debt to Equity reaching almost 0.6xFY2020E numbers and fully reflect in the FY2021 financials. The acquired business, as guided by the Management has EBDITA margins in line with APL (20-22%), making the deal attractive in terms of payback also. Transaction is expected to be accretive to normalized EPS from first full year of ownership and will augment the net profit growth by 20% on a full year basis. We maintain a Buy with a revised target of `870.

**Adds to Oral & Dermatology portfolio:** With this acquisition, Aurobindo would become the 2<sup>nd</sup> largest dermatology player in the US on both generic and branded dermatology products along with specialized manufacturing capabilities in creams, ointments, and other topical dosage forms. Acquisition will add approximately 300 products including projects in development as well as commercial and manufacturing capabilities in the US, complementing and expanding the group's portfolio and pipeline. The portfolio to be acquired has a revenue contribution of 70% from oral solids and 30% from dermatology.

The portfolio being divested generated sales of US\$0.6bn in 1HFY2018 for Sandoz. After expiration of certain in-licensed product contracts, and rationalizations of acquired products that will not negatively impact profitability (but before the impact of any potential FTC-led divestments) the portfolio is expected to generate over US\$0.9bn in sales for the first 12 months after completion of the transaction for Aurobindo.

**Synergy & Value creation opportunities a plus:** Apart from products, APL will add a dedicated derma salesforce, which covers ~75% of total prescriptions. The commercial infrastructure provides a platform to build strong relationships with 'Big 3 Buyer' groups and expand presence among mid-tier buying groups. Over 80% revenue contribution through sales to these customers. This would complement and expand APL's portfolio. In addition, the company has an opportunity to collaborate with leading companies to market in-license and Authorised Generics products. These benefits, coupled with vertically integrated, highly efficient manufacturing base can enhance the overall value creation and enhance the position of the acquired portfolio over the medium-term.

## BUY

CMP	`760
Target Price	`870

**Investment Period**      **12 Months**

Stock Info	
Sector	Pharmaceuticals
Market Cap (` cr)	44,503
Net Debt (` cr)	2,579
Beta	1.1
52 Week High / Low	809/527
Avg. Daily Volume	52,572
Face Value (`)	1
BSE Sensex	38,243
Nifty	11,537
Reuters Code	ARBN.BO
Bloomberg Code	ARBPI.IN

Shareholding Pattern (%)	
Promoters	51.9
MF / Banks / Indian FIs	15.9
FII / NRIs / OCBs	17.7
Indian Public / Others	14.5

Abs.(%)	3m	1yr	3yr
Sensex	8.7	20.7	53.6
Aurobindo Pharm:	40.3	1.9	7.7

### 3-year price chart



Source: Company, Angel Research

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**Outlook & Valuations:** On valuation front, the company paid almost 1xMarketCap/sales, which we believe given the size and scope of the business acquired is very attractive. In addition, the transaction will lead to net debt to Equity reaching almost 0.6x FY2020E numbers, still under comfortable levels. On the Operating front, the company guided that the acquired business has OPM is in line with the company's current OPMs (around 20-22%). Thus, even though the company will take debt for same, given the profitability, the deal will add to the company's EPS from the year of consolidation. In addition, company has guided that it takes normally 6-9 months for such deals to be done, so mostly it will start reflecting in 3QFY2020/4QFY2020. Thus, it will fully reflect in FY2021. We believe that the deal can add almost ~11% on EPS growth in FY2020, with major benefits reflecting in FY2021. Given the opportunity and Aurobindo Pharmaceuticals position in the global generic, we believe that the company still should give decent upsides on the stock. **Hence, we maintain our buy with a price target of ₹870.**

#### Key Financials

Y/E March (₹ cr)	FY2017	FY2018	FY2019E	FY2020E
<b>Net Sales</b>	<b>14,845</b>	<b>16,233</b>	<b>18,701</b>	<b>21,829</b>
% chg	8.3	9.4	15.2	16.7
<b>Net Profit</b>	<b>2,302</b>	<b>2,423</b>	<b>2,753</b>	<b>2,877</b>
% chg	13.7	5.3	13.6	4.5
<b>EPS (Rs)</b>	<b>39.4</b>	<b>41.5</b>	<b>47.1</b>	<b>49.3</b>
EBITDA Margin (%)	21.5	21.6	21.7	19.6
P/E (x)	19.3	18.3	16.1	15.4
RoE (%)	27.6	23.0	21.4	18.7
RoCE (%)	23.1	20.6	20.1	19.6
P/BV (x)	4.7	3.8	3.1	2.7
EV/Sales (x)	3.2	2.9	2.5	2.1
EV/EBITDA (x)	14.8	13.6	11.6	10.8

Source: Company, Angel Research Note: CMP as of September 7, 2018, FY2020 does not include the Acquisition

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<b>Disclosure of Interest Statement</b>	<b>Aurobindo Pharmaceuticals</b>
1. Financial interest of research analyst or Angel or his Associate or his relative	No
2. Ownership of 1% or more of the stock by research analyst or Angel or associates or relatives	No
3. Served as an officer, director or employee of the company covered under Research	No
4. Broking relationship with company covered under Research	No

**Ratings (Based on expected returns over 12 months investment period):**

*Buy (> 15%)*

*Accumulate (5% to 15%)*

*Neutral (-5 to 5%)*

*Reduce (-5% to -15%)*

*Sell (< -15%)*