

## Top Research Picks

- ➔ India Financials: Margin-cost based lending – a breather for banks

## Other Research

- ➔ Aurobindo Pharma (ARBP IN, BUY): Approval streak continues

18 December 2015



17 December 2015

# India Financials

## Margin-cost based lending – a breather for banks

To improve transmission of policy rates, the RBI has moved towards a new base rate formula, directing banks to price advances based on marginal cost of funds. The guidelines will be applicable on all loans sanctioned and renewed from Apr'16, unlike the draft guidelines which covered the entire loan book. Banks can publish base rates for different tenor loans and charge a tenor premium, thus reducing the margin impact amid a falling interest rate scenario. Banks can also reset their base rate up to one year.

The final guidelines are clearly diluted than the draft guidelines with lower margin impact for all corporate lenders like AXSB and ICICIBC, and PSBs.

- ➔ **Applicable on incremental/renewed loans:** The RBI has asked banks to price all new loans sanctioned or renewed from Apr'16 based on the Marginal Cost of Funds based Lending Rate (MCLR). Since these guidelines are applicable only on incremental loans, it will reduce the impact on bank margins. The central bank has also given an option to existing borrowers (currently linked to the base rate) to continue till repayment/renewal of loans or migrate to MCLR – a move which should also cushion bank margins.
- ➔ **Introduction of tenor premium:** The RBI has introduced tenor premium – a new component to be linked to the MCLR. Banks would have to publish their benchmark rates for multiple tenor loans ranging from overnight to one year on a monthly basis. This will allow them to charge higher-tenor premium to loans with a longer repayment period, reducing the volatility and impact on margins in a declining interest rate scenario.
- ➔ **Clause to reset base rate up to one year:** Banks have been given an option to offer floating loans with reset dates linked either to the loan sanction date or the date of MCLR review. Banks can reset their base rate for a maximum up to one year. Irrespective of the changes in the benchmark during the interim period, the same MCLR will be applicable till the next reset date. In our view, banks may classify certain loans towards the one-year reset period to reduce the margin impact. Since there is a lead-lag effect between re-pricing of deposits and loans, the longer the reset period, the lesser will be the margin impact.
- ➔ **Positive for corporate lenders:** These guidelines are clearly less stringent than the draft guidelines released in September, with only half the margin impact for corporate lenders. We think the guidelines should benefit the private banks such as AXSB and ICICIBC as well as PSU banks. In our view, the NIM impact for SBIN will be closer to 10bps-15bps as against 20bps-25bps estimated earlier. In contrast, retail-centric banks like HDFCB, KMB and IIB, which have fixed loans as high as ~50-70%, should see negligible margin impact.



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### Average maturity of deposits and advances as on FY15

Banks	Deposits	Advances
<b>Private sector banks</b>		
Axis Bank	2.7	3.3
HDFC Bank	2.4	1.8
ICICI Bank	2.8	2.4
IndusInd Bank	2.1	1.9
YES Bank	1.4	2.0
Kotak Bank	1.0	2.2
<b>Average</b>	<b>2.1</b>	<b>2.2</b>
<b>Public sector banks</b>		
SBI	2.3	1.9
Bank of Baroda	1.6	1.6
PNB	2.2	1.9
Bank of India	1.7	1.4
Canara Bank	1.3	2.0
Union Bank	2.8	1.9
<b>Average</b>	<b>2.0</b>	<b>1.8</b>

**BUY**

TP: INR 935.00

▲ 14.0%

## Aurobindo Pharma

ARBP IN

### Approval streak continues

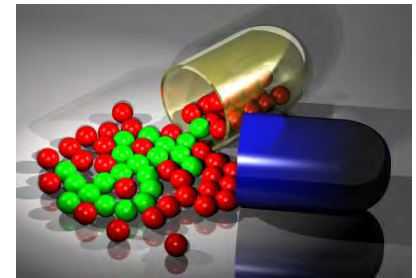
ARBP has received the USFDA's nod for *gSolu-Medrol* (methylprednisolone sodium succinate injection; market size: US\$ 102mn as per MAT Oct'15) and *gImodium A-D tablets* (Loperamide Hcl; market size: US\$ 9.7mn). We believe the *gMedrol* launch can be a substantive one, adding US\$ 15mn-20mn p.a. to revenues. With 33 approvals in FY16 YTD (including 2 tentatives), ARBP continues to defy the general industry trend of slower approvals. The stock is our top mid-cap pick – maintain BUY with a Sep'16 TP of Rs 935.

- ➔ **gMedrol can add US\$ 15mn-20mn annually to revenues:** Currently, two generics of *Medrol* – *Fresenius Kabi* and *Mustafa Nevsat* – are available in the market while a few others (*Bedford, Abraxis, Watson, Teva*) have been discontinued for various reasons. If current market dynamics prevail, *gMedrol* can add US\$ 15mn-20mn annually to ARBP's sales, assuming 30% incremental price erosion and 20-25% market share. **Having said that, we believe ARBP's launch of *gMedrol* is likely to be delayed by a couple of months, given the ongoing expansion at its unit IV, and the actual impact should be visible from FY17 onwards.**
- ➔ **Approval streak continues:** ARBP's tally of 33 approvals in FY16 YTD is the highest amongst Indian generics. In fact, the last few approvals have relatively better market dynamics (at least six approvals over the last six months have <4 players and a market size between US\$ 100mn and US\$ 400mn). Also, approval for *gAbilify* is substantial given the large market size of US\$ 7.3bn (Fig 1).
- ➔ **US segment to drive business momentum:** On a high base, we expect the US business to grow at a 22.7% CAGR over FY15-FY18 led by (a) a rising share of complex generics in the product mix, (b) a large ANDA pipeline (168 pending ANDAs), (c) strong growth in injectables/controlled substances, and (d) OTC penetration through the *Natrol* acquisition. Favourable market dynamics in some of the recent approvals can lead to healthy growth upside in our estimates.

### Financial Highlights

Y/E 31 Mar	FY14A	FY15A	FY16E	FY17E	FY18E
Revenue (INR mln)	80,873	121,205	149,369	169,347	187,429
EBITDA (INR mln)	21,195	25,636	33,404	39,411	45,491
Adjusted net profit (INR mln)	11,729	15,758	20,277	25,193	29,395
Adjusted EPS (INR)	20.1	27.0	34.8	43.2	50.4
Adjusted EPS growth (%)	299.1	34.4	28.7	24.2	16.7
DPS (INR)	1.5	0.5	1.0	1.0	1.0
ROIC (%)	20.9	19.6	21.2	21.6	22.5
Adjusted ROAE (%)	36.9	34.9	32.3	29.7	26.4
Adjusted P/E (x)	40.8	30.4	23.6	19.0	16.3
EV/EBITDA (x)	21.1	17.3	13.2	11.2	9.9
P/BV (x)	12.8	9.0	6.6	4.9	3.8

Source: Company, Bloomberg, RCML Research



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PRICE CLOSE (16 Dec 15)

INR 820.50

MARKET CAP

INR 479.1 bln

USD 7.2 bln

SHARES O/S

584.0 mln

FREE FLOAT

54.0%

3M AVG DAILY VOLUME/VALUE

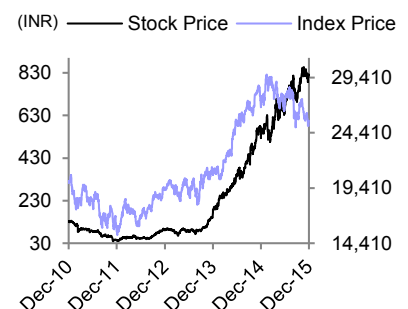
1.7 mln / USD 20.6 mln

52 WK HIGH

INR 861.55

52 WK LOW

INR 465.00



**BUY**

TP: INR 935.00

▲ 14.0%

**Aurobindo Pharma**

ARBP IN



Company Update

INDIA

PHARMACEUTICALS

**Per Share Data**

Y/E 31 Mar (INR)	FY14A	FY15A	FY16E	FY17E	FY18E
Reported EPS	20.1	27.0	34.8	43.2	50.4
Adjusted EPS	20.1	27.0	34.8	43.2	50.4
DPS	1.5	0.5	1.0	1.0	1.0
BVPS	64.3	90.8	124.4	166.5	215.7

**Valuation Ratios**

Y/E 31 Mar (x)	FY14A	FY15A	FY16E	FY17E	FY18E
EV/Sales	5.5	3.7	2.9	2.6	2.4
EV/EBITDA	21.1	17.3	13.2	11.2	9.9
Adjusted P/E	40.8	30.4	23.6	19.0	16.3
P/BV	12.8	9.0	6.6	4.9	3.8

**Financial Ratios**

Y/E 31 Mar	FY14A	FY15A	FY16E	FY17E	FY18E
<b>Profitability &amp; Return Ratios (%)</b>					
EBITDA margin	26.2	21.2	22.4	23.3	24.3
EBIT margin	22.3	18.4	19.1	20.0	20.9
Adjusted profit margin	14.5	13.0	13.6	14.9	15.7
Adjusted ROAE	36.9	34.9	32.3	29.7	26.4
ROCE	20.3	18.9	20.7	21.1	21.0
<b>YoY Growth (%)</b>					
Revenue	39.9	49.9	23.2	13.4	10.7
EBITDA	170.0	21.0	30.3	18.0	15.4
Adjusted EPS	299.1	34.4	28.7	24.2	16.7
Invested capital	26.2	25.0	20.3	12.8	9.6
<b>Working Capital &amp; Liquidity Ratios</b>					
Receivables (days)	96	93	96	99	100
Inventory (days)	97	90	97	99	100
Payables (days)	71	65	72	76	79
Current ratio (x)	1.5	1.6	1.8	2.2	2.7
Quick ratio (x)	0.0	0.1	0.0	0.1	0.3
<b>Turnover &amp; Leverage Ratios (x)</b>					
Gross asset turnover	2.0	2.5	2.4	2.4	2.3
Total asset turnover	1.0	1.1	1.1	1.1	1.0
Net interest coverage ratio	25.3	35.3	52.2	143.7	0.0
Adjusted debt/equity	1.0	0.7	0.5	0.3	0.1

**DuPont Analysis**

Y/E 31 Mar (%)	FY14A	FY15A	FY16E	FY17E	FY18E
Tax burden (Net income/PBT)	76.5	72.7	75.2	75.1	75.1
Interest burden (PBT/EBIT)	84.8	97.2	94.6	99.3	100.0
EBIT margin (EBIT/Revenue)	22.3	18.4	19.1	20.0	20.9
Asset turnover (Revenue/Avg TA)	98.1	111.3	110.4	108.6	104.6
Leverage (Avg TA/Avg equities)	259.5	240.9	215.7	184.0	160.9
Adjusted ROAE	36.9	34.9	32.3	29.7	26.4

**BUY**

TP: INR 935.00

▲ 14.0%

**Aurobindo Pharma**

ARBP IN



Company Update

INDIA

PHARMACEUTICALS

**Income Statement**

YE 31 Mar (INR mln)	FY14A	FY15A	FY16E	FY17E	FY18E
<b>Total revenue</b>	<b>80,873</b>	<b>121,205</b>	<b>149,369</b>	<b>169,347</b>	<b>187,429</b>
EBITDA	21,195	25,636	33,404	39,411	45,491
EBIT	18,070	22,310	28,522	33,799	39,148
Net interest income/(expenses)	(714)	(632)	(546)	(235)	19
Other income/(expenses)	0	0	0	0	0
Exceptional items	0	0	0	0	0
EBT	15,325	21,679	26,976	33,564	39,167
Income taxes	(3,635)	(5,966)	(6,744)	(8,391)	(9,792)
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	38	45	45	20	20
<b>Reported net profit</b>	<b>11,729</b>	<b>15,758</b>	<b>20,277</b>	<b>25,193</b>	<b>29,395</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>11,729</b>	<b>15,758</b>	<b>20,277</b>	<b>25,193</b>	<b>29,395</b>

**Balance Sheet**

Y/E 31 Mar (INR mln)	FY14A	FY15A	FY16E	FY17E	FY18E
Accounts payables	13,512	20,588	25,372	28,766	32,351
Other current liabilities	2,525	7,525	7,525	7,525	7,525
Provisions	1,358	1,101	1,440	1,440	1,440
Debt funds	37,691	42,626	38,546	31,466	24,886
Other liabilities	0	0	0	0	0
Equity capital	291	292	583	583	583
Reserves & surplus	37,210	52,627	71,934	96,448	125,163
Shareholders' fund	37,501	52,919	72,517	97,030	125,745
<b>Total liabilities and equities</b>	<b>92,844</b>	<b>124,971</b>	<b>145,566</b>	<b>166,374</b>	<b>192,076</b>
Cash and cash eq.	1,786	3,746	619	3,929	14,137
Accounts receivables	26,366	35,199	42,969	48,716	53,918
Inventories	23,675	36,196	42,969	48,716	53,918
Other current assets	12,375	9,962	14,323	16,239	17,973
Investments	198	198	198	198	198
Net fixed assets	27,217	38,943	44,060	48,448	52,106
CWIP	3,097	2,597	2,297	1,997	1,697
Intangible assets	0	0	0	0	0
Deferred tax assets, net	(2,054)	(2,054)	(2,054)	(2,054)	(2,054)
Other assets	184	184	184	184	184
<b>Total assets</b>	<b>92,844</b>	<b>124,971</b>	<b>145,566</b>	<b>166,374</b>	<b>192,076</b>

**Cash Flow Statement**

Y/E 31 Mar (INR mln)	FY14A	FY15A	FY16E	FY17E	FY18E
Net income + Depreciation	14,854	19,084	25,159	30,805	35,738
Interest expenses	714	632	546	235	(19)
Non-cash adjustments	2,031	0	0	0	0
Changes in working capital	(10,591)	(6,865)	(14,121)	(10,016)	(8,552)
Other operating cash flows	(544)	(48)	(45)	(20)	(20)
<b>Cash flow from operations</b>	<b>6,463</b>	<b>12,803</b>	<b>12,540</b>	<b>21,004</b>	<b>27,147</b>
Capital expenditures	(3,741)	(14,552)	(9,700)	(9,700)	(9,700)
Change in investments	(4,483)	0	0	0	0
Other investing cash flows	36	808	572	646	716
<b>Cash flow from investing</b>	<b>(8,187)</b>	<b>(13,744)</b>	<b>(9,128)</b>	<b>(9,054)</b>	<b>(8,984)</b>
Equities issued	35	0	0	0	0
Debt raised/repaid	2,675	4,935	(4,080)	(7,080)	(6,580)
Interest expenses	(1,071)	(1,439)	(1,118)	(881)	(697)
Dividends paid	(596)	(597)	(340)	(679)	(679)
Other financing cash flows	383	0	0	0	0
<b>Cash flow from financing</b>	<b>1,426</b>	<b>2,899</b>	<b>(5,538)</b>	<b>(8,640)</b>	<b>(7,956)</b>
<b>Changes in cash and cash eq</b>	<b>(299)</b>	<b>1,957</b>	<b>(2,126)</b>	<b>3,310</b>	<b>10,207</b>
<b>Closing cash and cash eq</b>	<b>1,786</b>	<b>3,746</b>	<b>619</b>	<b>3,929</b>	<b>14,136</b>

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