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Q1FY22 result review
and earnings revision

Pharmaceuticals

Target price: Rs2,000

EBITDA revision

(%)	FY22E	FY23E
Sales	(0.4)	0.3
EBITDA	(0.8)	0.6

Target price revision

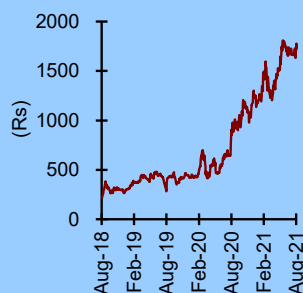
Rs2000 from Rs2,004

Shareholding pattern

	Dec '20	Mar '21	Jun '21
Promoters	44.1	44.1	44.1
Institutional investors	17.5	17.6	23.0
MFs and other	4.1	3.6	5.1
FIs/Insurance	0.0	0.1	1.0
FII	13.4	13.9	16.9
Others	38.4	38.3	35.9

Source: BSE India

Price chart



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INDIA

ICICI Securities

Solara Active Pharma Sciences

BUY

Maintained

Q1 miss; outlook intact

Rs1,724

Solara Active Pharma (Solara) reported Q1FY22 performance was below estimate due to demand pressure in some products including *Ibuprofen* in the regulated markets and temporary shutdown of plants due to COVID-19. Consolidated revenues grew 16.4% to Rs4.1bn led by strong growth in non-regulated markets, EBITDA margin was down 160bps YoY but flat QoQ to 22.5% due to lower proportion of regulated markets and adjusted PAT grew 19.9% to Rs507mn. We remain positive on the long term outlook considering presence only in the API and CRAMS space thereby removing any potential conflict with clients, maintaining large market share in key products, strong regulatory track record places Solara in a strong position to monetise the growing API business opportunities which would be augmented by the potential merger with Aurore Life. Reiterate BUY.

- **Growth driven by non-regulated markets, regulated markets dropped:** Solara reported a healthy revenue growth largely supported by growth in non-regulated markets which grew 228% YoY and 19.5% QoQ. Supplies from Vizag plant, where capacity utilisation is consistently increasing, to non-regulated markets was the key reason for this strong performance. However, regulated market reported a decline of 36.9% YoY due to demand pressure in certain key products including *Ibuprofen* and the same is expected to recover to normal levels in 2-3 quarters. Company expects to file 10-12 DMFs in FY22. This augurs well for the future growth of the API business. New products contribution increased to ~20% in Q1FY22 vs 8-10% in previous quarters. Solara added 4 new customers in CRAMS business in Q1FY22 and CRAMS business would grow over 50% in FY22E.
- **Margins stable and likely to improve:** Company reported a decline of 160bps YoY (+20bps QoQ) in EBITDA margin largely due to sharp jump in revenue from non-regulated markets which contributed ~57% to sales in Q1FY22 vs 20% YoY. This also led to gross margin decline of 100bps. Improving sales, higher utilisation and growing CRAMS business should all support margins in the future and we expect rise of 160bps to 25.5% over FY21-FY23E including Aurore.
- **Outlook:** We estimate Solara to report revenue, EBITDA and PAT CAGRs of 35.4%, 40.1% and 44.1% over FY21E-FY23E with higher demand for API and CRAMS, business boost post-merger with Aurore, and improving margin profile. We expect it to generate FCF of ~Rs4bn over FY22E-FY23E. While RoE and RoCE would be under pressure due to the merger with Aurore, excluding goodwill the ratios will remain strong at 21.9% and 19.1% respectively. The company expects revenue of Rs2.8bn with EBITDA margin of 23-25% in FY22 post Aurore merger.
- **Valuation and risks:** We largely maintain our estimates and maintain **BUY** with a revised target price of Rs2,000/share based on 13x FY23 EBITDA (earlier Rs2,004/share). **Key downside risks:** higher competition, currency fluctuations, and regulatory hurdles.

Market Cap	Rs61.9bn/US\$835mn
Reuters/Bloomberg	SOLA.BO/SOLARA IN
Shares Outstanding (mn)	35.9
52-week Range (Rs)	1811/852
Free Float (%)	45.9
FII (%)	16.9
Daily Volume (USD/'000)	3,291
Absolute Return 3m (%)	12.1
Absolute Return 12m (%)	103.2
Sensex Return 3m (%)	13.4
Sensex Return 12m (%)	45.9

Year to Mar	FY20	FY21	FY22E	FY23E
Revenue (Rs mn)	13,218	16,169	25,281	29,646
Net Income (Rs mn)	1,146	2,214	3,979	4,597
EPS (Rs)	31.9	61.6	80.9	93.4
% Chg YoY	92.5	93.2	31.2	15.5
P/E (x)	54.0	28.0	21.3	18.5
CEPS (Rs)	58.1	91.9	106.4	123.4
EV/E (x)	26.0	16.9	14.2	11.3
Dividend Yield (%)	0.3	0.3	-	-
RoCE (%)	11.7	15.4	13.9	11.1
RoE (%)	11.2	16.6	14.6	11.2

Please refer to important disclosures at the end of this report

Q1FY22 result and concall highlights

Net revenues grew 16.4% YoY to Rs4.1bn supported by growth in the non-regulated markets which grew 228% YoY while regulated markets declined 36.9% YoY in Q1FY22.

- The company has inducted new members to the board, notably Aditya Puri and Vineeta Rai. Aditya Puri (Former MD of HDFC Bank) joins the board as the Chairperson and Vineeta Rai (Former IAS officer and Revenue Secretary) joins as an Independent Director.
- The company aims to achieve a revenue growth CAGR of ~25% over the next 4 years. The company intends to register an EBITDA margin of 23-25% and record ROCE in excess of 20% over the coming years.

- **API** continues to be the key growth driver for the company supported by new product launches and entry into new markets. New products contributed ~20% to overall sales this quarter. The company sees strong demand visibility for new products in the next few quarters driven by firm customer commitments.

Company concluded 7 product development reports this quarter. Company expects to file 10-12 DMFs in FY22.

The regulated market saw a decline this quarter due to demand pressures in *Ibuprofen* and other base products. The company expects the base business to normalize over the next 2-3 quarters.

The company will be commercializing the backward integrated facility for *Ibuprofen* in Q3FY22.

- **CRAMS** business segment recorded a healthy growth for the quarter. The company sees strong revenue visibility in the segment with an indicated growth of over 50% YoY. Company has also added four new pharma clients this quarter, which is the highest quarterly addition in the last 3 years.
- **Gross margin** declined 100bps YoY (+390bps QoQ) to 56% due to increased raw material prices (especially *Ibuprofen*) and lower sales from regulated markets. **EBITDA margin** at 22.5% declined 160bps YoY due to increased contribution of non-regulated markets but increased 20bps QoQ due to an increase in gross margins.
- **R&D** costs for Q1FY22 stood at 3.5% of sales at Rs141mn. Capex during Q1FY22 was Rs490mn.
- **Adjusted PAT** grew 19.9% YoY to Rs507mn.

Table 1: Q1FY22 performance*(Rs mn, year ending March 31)*

	Q1FY22	Q1FY21	YoY % Chg	Q4FY21	QoQ % Chg
Net Sales	4,056	3,484	16.4	4,442	(8.7)
EBITDA	914	838	9.1	991	(7.8)
Other income	59	46	29.0	98	(39.6)
PBIDT	973	884	10.1	1,089	(10.6)
Depreciation	277	262	5.5	274	0.9
Interest	190	198	(4.4)	248	(23.6)
Extra ordinary income/ (exp.)	(6)	-		-	
PBT (before extraordinary)	501	423	18.4	566	(11.5)
Tax	-	1	(100.0)	0	(100.0)
Minority Interest	(0)	(0)		(0)	
Reported PAT	501	423	18.6	567	(11.5)
Adjusted PAT	507	423	19.9	567	(10.5)
EBITDA margins (%)	22.5	24.1	(160)bps	22.3	20bps

Source: Company data, I-Sec research

Table 2: Sales breakup*(Rs mn, year ending March 31)*

Segment Revenue	Q1FY22	Q1FY21	YoY % Chg	Q4FY21	QoQ % Chg
Regulated markets	1,779	2,818	(36.9)	2,586	(31.2)
Other markets	2,336	712	228.1	1,954	19.5
Net Sales	4,115	3,530	16.6	4,540	(9.4)

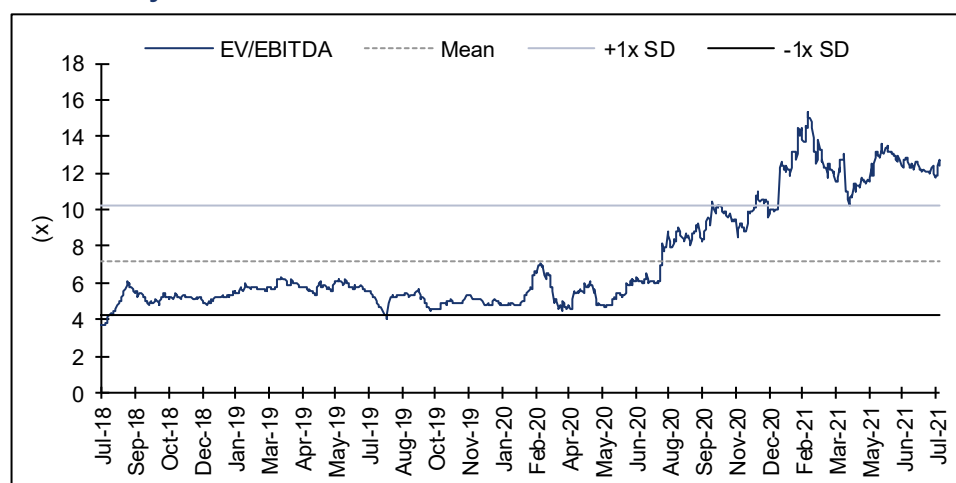
Source: Company data, I-Sec research

Valuations

We expect Solara to register EPS CAGR of 23.1% over FY21-FY23E, lower than PAT CAGR of 44.1% due to equity dilution on account of Aurore merger. This growth is driven by revenue CAGR of 35.4% and 160bps EBITDA margin improvement on high base of FY21. We believe revenue growth will be led by market share gain in existing products, new launches, merger of Aurore and strong growth in CRAMS business. We expect return ratios to remain low on account of merger with Aurore as it would create a large goodwill in the books.

The stock currently trades at valuations of 21.3x FY22E and 18.5x FY23E earnings and EV/EBITDA multiple of 14.2x FY22E and 11.3x FY23E. The stock has seen strong rerating in past one year, in line with other API companies, due to strong growth as witnessed in FY21 performance and potential opportunity from shift of API/CRAMS manufacturing to India given China disruptions. We believe current valuations are reasonable and so recommend **BUY** rating with a revised target price of Rs2,000/share based on 13x FY23E EBITDA (earlier: Rs2004/share based on 13x FY23E).

Chart 1: 1-year forward EV/EBITDA



Source: Company data, I-Sec research

Financial summary (consolidated)

Table 3: Profit & loss statement
(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Total Net Revenue	13,218	16,169	25,281	29,646
YoY Growth%	(4.7)	22.3	56.4	17.3
Total Op. Exp.	10,623	12,310	19,077	22,072
EBITDA	2,594	3,859	6,204	7,574
Margins %	19.6	23.9	24.5	25.5
YoY Growth%	17.5	48.7	60.8	22.1
Depreciation	942	1,087	1,255	1,474
EBIT	1,653	2,772	4,949	6,100
Other Income	275	288	288	288
Interest	779	845	816	782
EO Items	-	-	-	-
PBT	1,149	2,215	4,420	5,605
Tax	4	2	442	1,009
Tax Rate (%)	0.3	0.1	10.0	18.0
Minority Interest	(1)	(1)	(1)	(1)
Reported PAT	1,146	2,214	3,979	4,597
Adj. PAT	1,146	2,214	3,979	4,597
Net Margins (%)	8.7	13.7	15.7	15.5

Source: Company data, I-Sec research

Table 4: Balance sheet
(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
Paid-up Capital	269	359	492	492
Reserves & Surplus	10,591	15,526	38,077	42,674
Total Equity	10,859	15,885	38,569	43,166
Minority Interest	43	42	42	41
Total Debt	6,017	5,295	6,795	4,795
Deferred Liabilities	118	(256)	(256)	(256)
Capital Employed	17,037	20,967	45,150	47,746
Current Liabilities	4,498	4,913	7,347	8,456
Total Liabilities	21,534	25,880	52,497	56,202
Net Fixed Assets	14,374	14,696	34,645	35,671
Investments	3	4	4	4
Inventory	2,797	2,950	4,645	5,402
Debtors	2,265	4,839	6,809	7,586
Other Current Assets	1,527	1,406	2,996	3,213
Cash and Equivalents	568	1,985	3,398	4,326
Total Cur. Assets	7,157	11,180	17,848	20,527
Total Assets	21,534	25,880	52,497	56,202

Source: Company data, I-Sec research

Table 5: Cashflow statement
(Rs mn, year ending March 31)

	FY20	FY21	FY22E	FY23E
PBT (Adj. for Extraordinary)	1,149	2,215	4,420	5,605
Depreciation	942	1,087	1,255	1,474
Net Chg in WC	(260)	(1,760)	(1,888)	(740)
Taxes	(243)	(334)	(442)	(1,009)
Others	76	(499)	(933)	98
CFO	1,663	710	2,412	5,429
Capex	(2,676)	(1,715)	(2,500)	(2,500)
Net Investments made	(551)	500	-	-
Others	(361)	152	-	-
CFI	(3,588)	(1,063)	(2,500)	(2,500)
Change in Share capital	298	2,982	-	-
Change in Debts	1,636	(1,028)	1,500	(2,000)
Div. & Div Tax	(156)	(197)	-	-
Others	(49)	14	-	-
CFF	1,728	1,771	1,500	(2,000)
Total Cash Generated	(197)	1,418	1,412	929
Cash Opening Balance	765	568	1,985	3,398
Cash Closing Balance	568	1,985	3,398	4,326

Source: Company data, I-Sec research

Table 6: Key ratios
(Year ending March 31)

	FY20	FY21	FY22E	FY23E
Adj EPS	31.9	61.6	80.9	93.4
YoY Growth%	92.5	93.2	31.2	15.5
Cash EPS	58.1	91.9	106.4	123.4
EBITDA (%)	19.6	23.9	24.5	25.5
NPM (%)	8.7	13.7	15.7	15.5
Net Debt to Equity (x)	0.5	0.2	0.1	0.0
P/E (x)	54.0	28.0	21.3	18.5
EV/EBITDA (x)	26.0	16.9	14.2	11.3
P/BV (x)	5.7	3.9	2.2	2.0
EV/Sales (x)	5.1	4.0	3.5	2.9
RoCE (%)	11.7	15.4	13.9	11.1
RoCE (ex-goodwill) (%)	15.0	18.9	21.2	19.1
RoE (%)	11.2	16.6	14.6	11.2
RoE (ex-goodwill) (%)	17.5	22.8	25.7	21.9
RoIC (%)	12.2	16.5	15.1	12.0
Book Value (Rs)	302.3	442.2	783.7	877.1
DPS (Rs)	5.8	5.5	-	-
Dividend Payout (%)	13.6	8.9	-	-
Div Yield (%)	0.3	0.3	-	-
Asset Turnover Ratio	1.0	1.1	1.0	0.8
Avg Collection days	71	80	84	89
Avg Inventory days	150	145	121	138

Source: Company data, I-Sec research

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