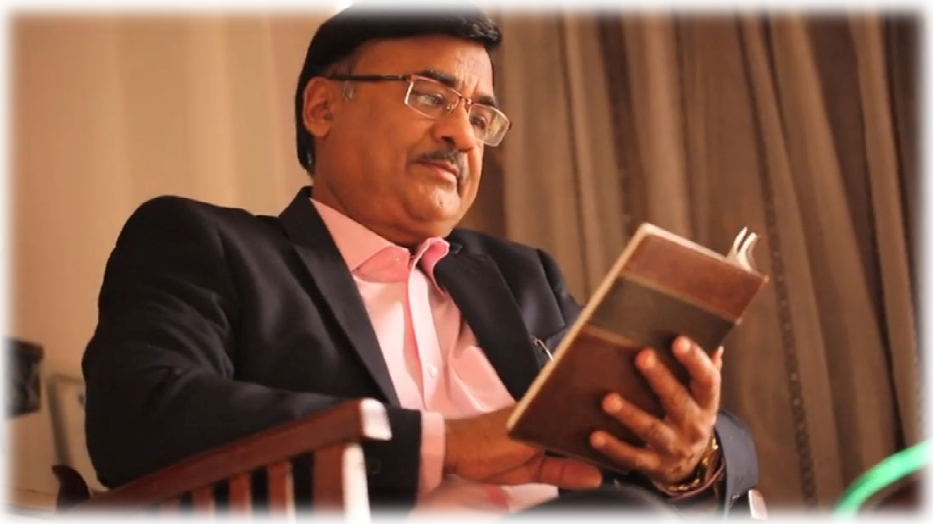
AJCON GLOBAL

YOUR FRIENDLY FINANCIAL ADVISOR



Dr. Ashok Ajmera (FCA), CMD & CEO

Dr. Ajmera's column as on June 16, 2018

Ongoing trade war between US and China to affect global markets; remain bullish on PSU Banking and pharma space..

Indian market ended the rangeboud week on a positive note with Nifty, Sensex gaining half-a-percent each. While Nifty ended above the crucial level of 10,800, Sensex ended above 35,600. The market traded in a narrow range amid domestic data including inflation data for the month of May while global cues include ECB meet, Fed meet. India's wholesale inflation grew 4.43 percent in May, a 14-month high, driven by some food items and fuel prices.

Domestic bourses ended flat on Friday amid weakness in their Asian peers that wobbled on Friday as investors braced for US tariffs against China. The S&P BSE Sensex ended at 35,622, up 22 points while the broader Nifty50 index settled at 10,818, up 10 points. Among sectoral indices, the Nifty Pharma index ended over 2% higher led by rise in the shares of Dr. Reddy's Laboratories, Cipla and Piramal Enterprises. The Nifty IT index too settled over 2% led by a rally in Infosys and Tata Consultancy Services (TCS). TCS hit a new high of Rs 1,849 per share on the BSE during the day, after the IT major said that its board has approved a proposal of buyback upto 76.19 million equity shares at price of Rs 2,100 per share through tender offer. The stock eventually settled 2.75 per cent higher at Rs 1841.45 on the BSE.

Nifty Pharma index was quoting higher for the eight straight trading days on the National Stock Exchange (NSE). During the period, the pharma index rallied 15% as compared to 2% rise in the benchmark Nifty 50 index. Dr Reddy's Laboratories, Lupin, Cadila Healthcare, Sun Pharmaceutical Industries, Aurobindo Pharma and Cipla from the Nifty Pharma index were up in the range of 8% to 14% thus far in the current week. Alembic Pharmaceuticals,

Granules India, Marksans Pharma, Ajanta Pharma and Suven Lifesciences, the non-index pharma gained between 9% and 20% during the week.

Dr Reddy's Labs was up 4% to Rs 2,365 on Friday (15th June, 2018), after the U.S. Food and Drug Administration (USFDA) approved the first generic versions of Indivior's Suboxone sublingual film for the treatment of opioid dependence. The stock rallied 14% so far in current week. Lupin gained 3% at Rs 923, too rallied 14% in past five trading sessions. The company on Thursday it has received approval from the US health regulator to market Drospirenone, Ethinyl Estradiol, Levomefolate Calcium tablets, used to prevent pregnancy, in the American market. While, during the week, Sun Pharma announced the resolution of regulatory compliance issues at Halol plant, Aurobindo Pharma gained on the back of US FDA (Food and Drug Administration) approval for Omeprazole (used to treat certain stomach and esophagus problems). Both these stocks have gained 8% so far in current week.

Foreign investors were net sellers as they sold equities worth Rs 5,294 crore, while domestic institutions were buyers in the last week as they bought equities worth Rs 4,014.25 crore. India's volatility index (India VIX) was down 5 percent last week. BSE Smallcap index was up 0.4 percent, BSE Midcap was ended flat and largecap index was up 0.4 percent.

Domestically, India's trade deficit widened to four-month high of US$14.62 billion in May as imports surged nearly 15 per cent, the government said Friday. Commerce Minister Suresh Prabhu said exports in May rose by 28.18 per cent to US$28.86 billion while imports were up 14.85 per cent to $43.48 billion. A rise in receipts of petroleum, engineering and pharmaceutical products boosted May's export growth figures to a six-month high of 20.18 per cent, up from 5.71 per cent in April. Even then the trade deficit widened to a four-month high of $14.62 billion, compared to the $13.7 billion deficit in April as imports rose by 14.85 per cent during the month, compared to the 4.60 per cent rise in April. This could pressurise the current account deficit in the first quarter of the current financial year after it stood at 1.9 per cent of GDP in the fourth quarter of 2017-18, compared to 2.1 per cent in the third quarter. However, within exports, major labour-intensive sectors, such as gems and jewellery and ready-made garments, continued to see declines. The export growth rate had peaked at over 30 per cent in November last year. Since then, the rate has fallen continuously until March. However, growth in outbound trade strengthened in May, with India exporting goods worth US$28.86 billion.

After major refining units remained shut for over two months, India finally managed to take advantage of rising global crude oil prices in May when petroleum exports rose by over 104 per cent to $5.23 billion. It had declined by 4.48 per cent in April. The same rising oil prices led to a much higher import bill of US$43.48 billion in May 2018. A major part of this was due to the US$11.5 billion crude oil import bill, which jumped nearly 50 per cent, up from the 41 per cent rise in April.

US President Donald Trump has decided to impose "pretty significant" tariffs and will announced a list targeting US$50 billion of Chinese goods on Friday, and a second wave of

products worth US$100 billion has been cued up. China retaliated against planned US tariffs on Chinese goods by targeting high-value American exports — including farm products, cars, and crude oil — bringing the world's two biggest economies closer to an all-out trade war. Shortly after the Trump administration unveiled plans Friday to impose tariffs of 25% on US$50 billion in Chinese products, China's State Council announced it would levy penalties of the same rate on the US goods of the same value. In striking back at the US action, China expanded the list of US products that would be subject to tariffs to 659 types of goods, from some 106 types it originally disclosed in April. Most of the added goods on China's retaliatory list are agricultural, seafood and energy products. President Donald Trump said earlier Friday that the US would respond with more tariffs if China retaliated.

India also has submitted a revised list of 30 items -- including motorcycle, certain iron and steel goods, boric acid and lentils -- to the WTO on which it proposes to raise customs duty by up to 50 per cent. As duties hiked by the US on certain steel and aluminium products would have implications of about $241 million on India, the raise in tariffs proposed by New Delhi too would have an equal implication on America. Earlier in May, India proposed to raise duties by up to 100 per cent on 20 products such as almonds, apple and specific motorcycles imported from the US. The additional duty proposed to be hiked on these items ranges from 10 per cent to 100 per cent.

Global Markets

The US Federal Reserve, on Thursday, had raised interest rates and took a more hawkish tone in forecasting a slightly faster pace of tightening for the rest of the year.

Globally, the Asia Pacific MSCI index ex-Japan edged down 0.3 per cent and was set for a weekly loss of more than 1 per cent.

European shares were set for their best week in more than three months as investors pushed back expectations for an interest rate increase after Thursday's European Central Bank meeting. The pan-European STOXX 600 index fell 0.2 percent, up 2.2 percent on the week, as recovering euro weighed. The euro was headed for its worst weekly loss in 19 months after the ECB signalled interest rates would be left at record lows into at least mid-2019. The common currency shed 1.9 percent to the dollar, its biggest daily decline since Britain voted to quit the EU in 2016. The drop in the euro gave a lift to the dollar, which hit its highest against a basket of currencies since November 2017. While the Federal Reserve and the ECB provided much of the week's central bank fireworks, the Bank of Japan produced no surprises at the end of a two-day policy meeting on Friday and looked set to continue its asset purchases for some time.

Chinese stocks led the losses, with the benchmark Shanghai Composite index plumbing a 20-month low, as investors worried about the economic damage from the trade tensions with the US. Japan's Nikkei average closed up 0.5 per cent.

Oil prices were little changed as investors eyed a key OPEC meeting in Vienna. Saudi Arabia and Russia, architects of a producer deal to cut output, have indicated they want production to rise.

Ajcon's view

At Ajcon Global, we believe most of the quality names are available in large cap space. Midcaps have been witnessing consistent hammering post Union Budget 2018-19 and SEBI re-allocation dictum for Mutual Fund industry. No doubt, midcaps and smallcaps have delivered excellent set of returns before this downfall. However, investors need to be careful while selecting stocks in midcap space as any unfavourable result in state elections would result in a drastic fall in midcaps and smallcaps space.

At present, we believe stocks from PSU Banking space and defensive space like Pharma can do well as we feel this sector has bottomed out. One can accumulate companies in pharma for 2-3 years horizon as it will get rerarted when earnings become visible. Shares of pharmaceutical companies were on a roll last week with the Nifty Pharma index posted its biggest weekly gain in 15 years following the positive news flow from the corporate levels with regard to US regulatory issues.

Top picks

Sun Pharma

We believe Sun Pharma is the best play in Pharma space and investors can add this stock in the long term portfolio. At CMP, of Rs. 571 (Face Value: Re. 1), the stock trades at a P/E of 52x on FY18 EPS which seems expensive in the near term after the recent rally. However, considering the long term prospects of the Company and expected approvals of its products pipeline post the clearance of Halol (after nearly 3 years of non compliance with USFDA), we believe investors will be rewarded in the longer term. Halol facility is carrying a USFDA warning letter since December 2015. Please note that a warning letter is issued to a manufacturing site if the manufacturer fails to address the violations of good manufacturing practices raised by the US drug regulator to its satisfaction. Though the warning letter doesn't restrict the company from selling products already approved, but it blocks new approvals. Halol plant was engaged in manufacturing every formulation including tablets, capsules, liquids, sterile dry powder injectable, small volume injectable, ointments, soft gelatine caps andaerosols, among others. It has approvals from key regulators such as USFDA, MHRA (UK), MCC (SA). In FY15, the site accounted for about USD 400 million of sales, which was nearly 15 percent of the company's total sales, before the warning letter was issued. But since then the sales from the plant have fallen to 8-10 percent of the total sales. In fact, the entire injectable portfolio was filed from Halol site that held key for Sun Pharma's future growth.

The company is transforming itself from being a generic player to a speciality one and has 3 major drugs in its pipeline namely tildrakizumab, OTX101 and a newly approved oncology drug "Yonsa". Ideally, it would take 2-3 years time for these products to rampup and contribute significant to sales. Remember, Sun Pharma is one of the pioneers among Indian pharmaceutical companies to see tremendous value in investing in research & development (R&D). The Company's early investments in R&D, beginning three decades ago, enabled it to make technology its key differentiator and develop a basket of robust products for diverse markets across the world. The Company has around 2000 research scientists working in multiple R&D centres equipped with cutting-edge enabling technologies for

research. The Company's scientists have expertise in developing generics, difficult to make technology intensive products, Active Pharmaceutical Ingredients (APIs), Novel Drug Delivery Systems (NDDS) and New Chemical Entities (NCEs). The Company has 422 ANDA's approved and 139 pending ANDA approvals.

The Company has over 40 (API & finished dose) state-of-the-art manufacturing sites spanning 6 continents. These manufacturing units are located in India, the US, Brazil, Canada, Egypt, Hungary, Israel, Bangladesh, Mexico, Romania, Ireland, Morocco, Nigeria, South Africa and Malaysia. The units ensure that we are able to provide best-in-class products to patients across 150 countries worldwide. The manufacturing operations are focused on producing generics, branded generics, speciality, over-the-counter (OTC) products, anti-retrovirals (ARVs), Active Pharmaceutical Ingredients (APIs) and intermediates in the full range of dosage forms, including tablets, capsules, injectables, ointments, creams and liquids. The Company also manufacture speciality APIs, including controlled substances, steroids, peptides and anti-cancers. The Company has a diversified revenue mix with US Formulations accounting (45%), India Branded Formulations (26%), Emerging Markets (15%), Western Europe and other markets (9%) and API & others (5%).

The Company's US business was under pressure since the warning letter issued by USFDA for Halol facility, as it has not received any product approval from Halol facility in three and a half years. The facility contributes 8-10% of US sales for the Company, currently - down from >15% at the time of warning letter. The facility's contribution later declined to about $250 million. The Company said on June 12 that it had received the Establishment Inspection Report (EIR) from the US Food and Drug Administration (FDA) for its crucial Halol facility in Gujarat indicating a closure of inspection. "The agency concluded that the inspection is now closed and the issues contained in the Warning Letter issued in December 2015 have been addressed," Sun Pharma said in a statement to stock exchanges. "This is an important development for Sun Pharma. We remain committed to following the highest levels of quality and 24x7 cGMP compliance at all our manufacturing facilities globally," the company said. The EIR will allow Sun Pharma to restart supplies from the Halol facility to the US. US alone has contributed around 40 percent of Sun Pharma overall sales in FY18. US revenue had witnessed adegrowth 34 percent on yoy basis - as the company was struggling with pricing pressure in that market. We believe the current resolution of the Halol issue would augur well for the Company. We can expect visibility on key approvals including Xelpros, Elepsia, Vagifem, etc. Going forward, focus of the Company will shift to its specialty pipeline (Llumya, Yonsa and Seciera to launch in FY19). Going it is looking to launch 3 speciality generic product like Yonsa (Q1FY19),Tildrakizumab (IL-23)(inQ2FY19)andOTX-101(possiblyH2FY19). The company has also received approval for gGlumetza and will be commercializing it in US soon. In addition, we believe improvement in Taro's US business along with the rampup in non US markets such Europe, emerging markets and India business will help to sustain the margins.

Dr. Reddy's

Dr. Reddy's is an integrated pharmaceutical company, committed to providing affordable and innovative medicines for healthier lives. Through its three businesses - Pharmaceutical Services & Active Ingredients, Global Generics and Proprietary Products - Dr. Reddy's offers a portfolio of products and services including APIs,

custom pharmaceutical services, generics, biosimilars and differentiated formulations. The Company's major therapeutic areas of focus are gastrointestinal. cardiovascular, diabetology, oncology, pain management and dermatology. Dr. Reddy's operates in markets across the globe. It's major markets include - USA, India, Russia & CIS countries, and Europe. At CMP of Rs. 2,351 (Face Value: Rs. 5), the Company is valued at a P/E of 40x on FY18 EPS. Investors can consider this Company for 3 years horizon. The performance of the earnings is dependent upon timely approvals of its products in pipeline.

The company recently announced that it has received an approval from US FDA and is launching Buprenorphine and Naloxone Sublingual Film, a therapeutic equivalent generic version of Suboxone. Buprenorphine and naloxone are used to treat adults with opioid addiction. "Buprenorphine helps suppress withdrawal symptoms caused by discontinuation of opioid drugs, and naloxone reverses and blocks the effect of opioids. This combination of medications is used as part of a complete treatment program including prescription monitoring, counseling, and psychosocial support," the company said in a filing to the exchanges. The Suboxone brand had US sales of approximately US$1.86 billion for the most twelve months ending in April 2018 according to IMS Health.

Dr Reddy's said it's launching generic Suboxone at risk - implying that the company is launching the product even as certain patent granted to the innovator is valid until 2023. Indivior has sued Dr Reddy's for infringement of its patents and litigation is still on. The Company is confident after recent court verdict going against Indivior, and delayed assertion of new patents, and two of the three patents being just an extension of old patents. Dr Reddy's also faces the risk of Indivior getting an injunction. In the worst case scenario if Dr Reddy's loses patent litigation, it may have to forfeit sales made on the drug. Dr Reddy's bought Suboxone Film's abbreviated new drug application (ANDA) from Teva Pharmaceuticals for USD 70 million in June 2016 with seven generic filers. Mylan too got an approval from USFDA to launch generic Suboxone. It's not immediately known whether Mylan will launch it immediately or wait till 2023. Mylan had a out of court settlement with Indivior on Suboxone. Alvogen, Endo, Par Pharmaceuticals and Actavis are also in the race for US FDA approval, some of them have settled patent infringement cases with Indivior to launch an authorised generic.

Natco Pharma

Incorporated in 1981 and headquartered in Hyderabad with over 4,825 employees across all locations, the Company is a niche player with R&D focussed, vertically integrated with an experienced management team and presence across multiple speciality therapeutic segments. Focused on complex generics for the US markets with niche Para IV and Para III filings. Integrated platform makes Natco a low cost manufacturer while strong global presence establishes them as a prospective player. Natco enjoys an API portfolio of more than 37 US DMFs (submission of details to FDA) with over 10 products under development. The Company has 43 niche ANDA filings including 20 Para IV filings in the US – with 22 approved ANDAs. Natco through its partner Mylan is expecting to generate significant sales from gCopaxone 40mg in FY19. Note gCopaxone is used for the treatment of people with relapsing forms of multiple sclerosis (MS). Through their another partner Alvogen which launched gTamiflu suspension for the first time in last year is expected to boost revenue growth during the flu season(typically Nov- March).

According to the management in its recent concall, in Q4FY18, the Company benefited from the strong flu season in the US market. Company has gTamiflu (suspension and tablet) in the market. gTamiflu revenue in Q4FY18 was high and some profit will also get recognized in Q1FY19E. gCopaxone is slow ramping product but a sticky product and will drive profitability in FY19E, current market share at 15-16% and management expects less competition. The 20mg gCopaxone is manufactured in India, while 40mg gCopaxone is manufactured at contracted side. In gVidaza, market share is 7-8% but it is not a large product, in gFosrenol (lanthanum carbonate - used to lower phosphate levels in patients with end stage kidney disease.), Natco is the only generic player. In gRevlimid, Natco has send response to USFDA queries and expects to submit the drug to FDA and approval is likely by end of FY19E end early FY20E.

In Q4FY18, formulation revenue ex-US stood at Rs. 158.5 crs. (Oncology – Rs. 82.8 crs., non-oncology Rs62.4crs.), API revenue stood at Rs. 60 crores and export formulation (incl. profit sharing) Rs. 492 crs. In domestic oncology, Natco has launched some first-to-launch drugs, Hep-C franchisee is stabilizing. Hep-C franchisee will grow further when it gets approvals in Indonesia and Philippines. The Management believes that only niche products will make money in the US market. Over next few years, company has said that it has few one off large opportunities in US. It expects approval momentum to tick in Brazil from FY19E onwards. Going ahead, India, Brazil and Canada will remain focus areas and company has said that it will keep focussing on the niche areas. Canada business has a top-line of Canadian US$15mn. and is profitable.

We believe the Company is executing well and is one of the best niche play in pharma industry. The Company boasts of strong brand position in the domestic Oncology and Hepatitis – C ('Hep-C') segments. The Company launched the generic version of Gilead's Sovaldi (Sofosbuvir) and its combinations for the treatment of Hep-C in India. Over the last couple of years the Company has proved its R&D capabilities and successfully launched multiple complex generics. The Company has witnessed a stellar run in its profitability at PAT level from Rs. 157 crores in FY16 to Rs. 695 crores in FY18. The Company has a strong balance sheet and has a robust base to make relatively aggressive investments (vs the past) to move into the next growth orbit. We expect strong earnings growth owing to the anticipated launches of gNexavar and gRevlimid along with gCopaxone. The Company is intensifying regulatory filings rate in RoW markets led by Hep-C portfolio. The Company is focused on a select few high-potential filings, predominantly differentiated products through either Novel Drug Delivery Systems (NDDS) or complex chemistries. With the scale-up in India and RoW markets, the Company is bound to witness healthy run in the next 3-5 years. For FY18, ROE and ROCE stood at 22.6 percent and 28.9 percent respectively. At CMP of Rs. 830 (Face value: 2), the Company is valued at 21x on FY18 EPS which we believe is cheap as compared to its peers. Long term investors are recommended to add this Company in portfolio and wait for atleast 5 years to reap the rewards of wealth creation.

Dr. Ashok Ajmera, FCA

AJCON GLOBAL
YOUR FRIENDLY FINANCIAL ADVISOR

Disclaimer

Ajcon Global Services Ltd. is a fully integrated investment banking, merchant banking, corporate advisory, stock broking, commodity and currency broking. Ajcon Global Services Ltd. research analysts responsible for the preparation of the research report may interact with trading desk personnel, sales personnel and other parties for gathering, applying and interpreting information.

Ajcon Global Services Ltd. is a SEBI registered Research Analyst entity bearing registration Number INH000001170 under SEBI (Research Analysts) Regulations, 2014.

Individuals employed as research analyst by Ajcon Global Services Ltd. or their associates are not allowed to deal or trade in securities that the research analyst recommends within thirty days before and five days after the publication of a research report as prescribed under SEBI Research Analyst Regulations.

Subject to the restrictions mentioned in above paragraph, we and our affliates, officers, directors, employees and their relative may: (a) from time to time, have long or short positions acting as a principal in, and buy or sell the securities or derivatives thereof, of Company mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage.

Ajcon Global Services Ltd. or its associates may have commercial transactions with the Company mentioned in the research report with respect to advisory services.

The information and opinions in this report have been prepared by Ajcon Global Services Ltd. and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of Ajcon Global Services Ltd. While we would endeavour to update the information herein on a reasonable basis, Ajcon Global Services Ltd. is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent Ajcon Global Services Ltd. from doing so. This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. Ajcon Global Services Ltd. will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. Ajcon Global Services Ltd. accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice. Ajcon Global Services Ltd. or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

AJCON GLOBAL
YOUR FRIENDLY FINANCIAL ADVISOR

Ajcon Global Services Ltd. encourages independence in research report preparation and strives to minimize conflict in preparation of research report. Ajcon Global Services Ltd. or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither Ajcon Global Services Ltd. nor Research Analysts have any material conflict of interest at the time of publication of this report.

It is confirmed that CA Ashok Ajmera or any other Research Analysts of this report has not received any compensation from the company mentioned in the report in the preceding twelve months. Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

Ajcon Global Services Ltd. or its subsidiaries collectively or Directors including their relatives, Research Analysts, do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.
It is confirmed that CA Ashok Ajmera research analyst or any other Research Analysts of Ajcon Global do not serve as an officer, director or employee of the companies mentioned in the report.

Ajcon Global Services Ltd. may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor Ajcon Global Services Ltd. have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on Ajcon Global Services Ltd. by any Regulatory Authority impacting Equity Research Analysis activities.

Analyst Certification

I, CA Ashok Ajmera, research analyst, author and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject securities. I also certify that no part of compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view (s) in this report.

For research related queries contact:

Mr. Akash Jain – Vice President (Research) at research@ajcon.net

CIN: L74140MH1986PLC041941

SEBI registration Number: INH000001170 as per SEBI (Research Analysts) Regulations, 2014.

Website: www.ajcononline.com

Corporate and Broking Division : 408 - (4th Floor), Express Zone, "A" Wing, Cello – Sonal Realty, Near Oberoi Mall and Patel's, Western Express Highway, Malad (East), Mumbai – 400063. Tel: 91-22-67160400, Fax: 022-28722062

Registered Office: 101, Samarth, Off. Hinduja Hospital, 151 Lt. P.N. Kotnis Road, Mahim (West), Mumbai – 400016. Tel: 022-24460335/36/40