

**BUY**

TP: Rs 1,650 | ▲ 15%

**AJANTA PHARMA**

Pharmaceuticals

20 May 2020

## Near-term growth concerns but demand outlook intact

**Ajanta Pharma (AJP) posted strong Q4 revenue/EBITDA growth of 32%/31% YoY to Rs 6.8bn/Rs 1.7bn. However, margins declined both YoY and QoQ to 24.4% due to higher other costs (as the Dahej oral dosage unit & Pithampur block were operationalised). Region-wise, India and US sales were steady while Asia made a strong return to normalised growth. Reported PAT stood at Rs 1.3bn. AJP is guiding for healthy operating leverage in FY21, starting Q3. We assume coverage with BUY and a Mar'21 TP of Rs 1,650, based on 16x FY22E EV/EBITDA.**

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**BUY with TP of Rs 1,650:** We expect a stable brand franchise (India & EM), US operating leverage and capex moderation to drive a 15%+ EPS CAGR for AJP over FY20-FY23. With over 75% of FY21/FY22 EPS estimated to accrue from the branded business, improving FCF and 30%+ ROIC beyond FY22E, we see scope for valuation upsides. We assume coverage with BUY and a Mar'21 TP of Rs 1,650 set at 16x FY22E EV/EBITDA (24x implied P/E). We like AJP for its (1) rational capital allocation, (2) capable management, (3) robust brand franchise, (4) flawless cGMP compliance, and (5) resilient margins & return ratios.

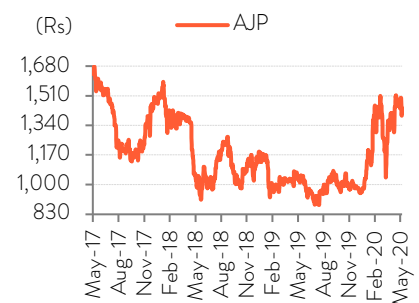
**Near-terms concerns for India business:** India sales grew 11% YoY in Q4 with dermatology and ophthalmology showing some sluggishness due to Covid-19 challenges. AJP believes the extended lockdown could hurt India growth in the near term, but that export formulations should continue to drive visibility with two blocks being operationalised in Q4. US sales were at US\$ 20mn (-10% QoQ) while Asia grew 46% YoY (on a low base) and 32% QoQ.

**Other takeaways:** (1) FY20 debtors spiked 68% or Rs 3.1bn due to increased US business. (2) Other income includes Rs 450mn forex gain. (3) FY21 capex is at Rs 2bn (incl. Rs 1bn maintenance capex). (4) Plans to file 10-12 ANDAs in FY21.

Ticker/Price	AJP IN/Rs 1,439
Market cap	US\$ 1.7bn
Shares o/s	88mn
3M ADV	US\$ 3.7mn
52wk high/low	Rs 1,580/Rs 825
Promoter/FPI/DII	71%/9%/9%

Source: NSE

## STOCK PERFORMANCE



Source: NSE

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
Total revenue (Rs mn)	21,320	20,553	26,183	27,684	31,339
EBITDA (Rs mn)	6,581	5,653	6,996	7,389	8,602
Adj. net profit (Rs mn)	4,686	3,869	4,412	4,915	6,047
Adj. EPS (Rs)	53.4	44.1	50.3	56.0	68.9
Adj. EPS growth (%)	(9.8)	(17.4)	14.0	11.4	23.0
Adj. ROAE (%)	25.8	17.8	17.9	17.3	18.4
Adj. P/E (x)	26.9	32.6	28.6	25.7	20.9
EV/EBITDA (x)	19.2	22.2	17.9	16.9	14.4

Source: Company, BOBCAPS Research

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**FIG 1 – QUARTERLY PERFORMANCE**

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20P	FY19
<b>Net Sales</b>	<b>6,820</b>	<b>5,151</b>	<b>32.4</b>	<b>6,512</b>	<b>4.7</b>	<b>25,878</b>	<b>20,552</b>
<b>EBITDA</b>	<b>1,664</b>	<b>1,271</b>	<b>31.0</b>	<b>1,861</b>	<b>(10.6)</b>	<b>6,988</b>	<b>5,586</b>
Depreciation	260	187	-	236		956	721
<b>EBIT</b>	<b>1,404</b>	<b>1,084</b>	<b>29.6</b>	<b>1,625</b>	<b>(13.6)</b>	<b>6,032</b>	<b>4,865</b>
Interest	36	8	-	16	-	119	12
Other Income	116	16	-	146	-	470	293
<b>PBT</b>	<b>1,484</b>	<b>1,092</b>	<b>35.9</b>	<b>1,755</b>	<b>(15.4)</b>	<b>6,384</b>	<b>5,146</b>
Less: Taxation	470	202	-	675	-	1,964	1,271
Less: Minority Interest	-	-	-	-	-	0	0
<b>Recurring PAT</b>	<b>1,014</b>	<b>890</b>	<b>13.9</b>	<b>1,080</b>	<b>(6.1)</b>	<b>4,420</b>	<b>3,875</b>
Exceptional items	275	0	-	(3)	-	261	0
<b>Reported PAT</b>	<b>1,289</b>	<b>890</b>	<b>44.8</b>	<b>1,077</b>	<b>19.7</b>	<b>4,681</b>	<b>3,875</b>
<b>Key Ratios (%)</b>							
Gross Margin	74.0	79.5	-	74.0	-	74.7	81.4
EBITDA Margin	24.4	24.7	-	28.6	-	27.0	27.2
Tax / PBT	31.7	18.5	-	38.5	-	30.8	24.7
NPM	14.9	17.3	-	16.6	-	17.1	18.9
<b>EPS (Rs)</b>	<b>11.6</b>	<b>10.2</b>	<b>-</b>	<b>12.3</b>	<b>-</b>	<b>50.4</b>	<b>44.2</b>

Source: Company, BOBCAPS Research

**FIG 2 – REVENUE MIX**

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20P	FY19
Domestic Formulation	1,770	1,590	11.3	1,950	(9.2)	7,690	6,900
Export Formulation	4,900	3,430	42.9	4,480	9.4	17,890	13,250
Africa	1,380	1,210	14.0	1,300	6.2	5,950	5,020
Asia	2,090	1,430	46.2	1,580	32.3	6,740	5,280
US	1,430	760	88.2	1,590	(10.1)	5,150	2,830
Others/LATAM	-	30	(100.0)	10	(100.0)	50	120
Other Op Income	150	131	14.5	146	2.7	504	382
<b>Revenues</b>	<b>6,820</b>	<b>5,151</b>	<b>32.4</b>	<b>6,576</b>	<b>3.7</b>	<b>26,084</b>	<b>20,532</b>

Source: Company, BOBCAPS Research

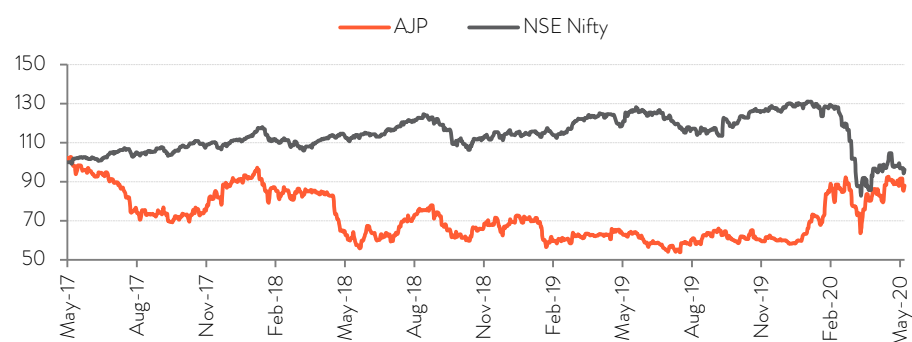
## Valuation methodology

AJP has a strong track record in terms of rational capital allocation, building a brand franchise, flawless cGMP compliance and stable returns ratios. We believe the branded generic franchise (India and EM) is strong and likely to remain resilient – this alongside operating leverage in the US business should drive an accelerated 15%+ EPS CAGR over FY20-FY23 (vs. flat growth for FY18-FY20).

In FY18, the company embarked on a major capex drive worth Rs 11bn towards augmenting formulation capacity, which is now nearing an end and should fuel a doubling of current sales, per management. We expect improved FCF momentum over the next 2-3 years based on healthy earnings growth and a normalised capex run-rate of Rs 1bn annually. Hence, ROIC levels are forecast to expand from 25% in FY19 to 33% by FY23.

At CMP, the stock is trading at 14x FY22E EBITDA (15% below the five-year mean) and 21x P/E which looks reasonable. We assume coverage on AJP with BUY and a Mar'21 target price of Rs 1,650, set at 16x FY22E EV/EBITDA (24x implied P/E).

**FIG 3 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

- **Concentration and regulatory risk in India business:** AJP's domestic formulation business is concentrated around three key therapies – ophthalmology, cardiology and dermatology – which drive 90% of sales. Any adverse regulatory action here can slow down overall business momentum. Current portfolio under price control is at 13% of India sales vs. 16% for industry.
- **US execution:** We estimate that the US business will contribute a third of our EPS over the next three years. This is mainly dependent on two key units – Paithan (~90% of existing US sales) and Dahej (future growth driver). Establishment inspection reports (EIR) for both units are in place (last inspected in Jul-Aug 19). Thus, ensuring strong cGMP compliance is key.
- **Slower offtake in branded generic exports:** Currency devaluation and repatriation concerns will lead to slower growth in branded generics markets.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
<b>Total revenue</b>	<b>21,320</b>	<b>20,553</b>	<b>26,183</b>	<b>27,684</b>	<b>31,339</b>
EBITDA	6,581	5,653	6,996	7,389	8,602
Depreciation	595	720	972	1,059	1,133
EBIT	5,987	4,933	6,025	6,330	7,469
Net interest income/(expenses)	(4)	(12)	(23)	(52)	(78)
Other income/(expenses)	242	210	370	364	671
Exceptional items	0	0	0	0	0
EBT	6,224	5,132	6,372	6,642	8,062
Income taxes	1,539	1,263	1,960	1,727	2,016
Extraordinary items	0	0	261	0	0
Min. int./Inc. from associates	0	0	0	0	0
<b>Reported net profit</b>	<b>4,686</b>	<b>3,869</b>	<b>4,673</b>	<b>4,915</b>	<b>6,047</b>
Adjustments	0	0	261	0	0
<b>Adjusted net profit</b>	<b>4,686</b>	<b>3,869</b>	<b>4,412</b>	<b>4,915</b>	<b>6,047</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Accounts payables	2,496	2,252	3,600	3,034	3,434
Other current liabilities	676	944	1,309	1,384	1,567
Provisions	418	383	488	516	584
Debt funds	10	340	428	1,300	1,300
Other liabilities	0	0	0	0	0
Equity capital	177	175	175	175	175
Reserves & surplus	20,477	22,545	26,335	30,267	35,105
Shareholders' fund	20,654	22,721	26,511	30,442	35,280
<b>Total liabilities and equities</b>	<b>24,254</b>	<b>26,640</b>	<b>32,336</b>	<b>36,676</b>	<b>42,165</b>
Cash and cash eq.	930	1,004	1,846	5,327	8,611
Accounts receivables	4,597	4,594	7,750	6,826	7,727
Inventories	3,506	4,357	4,950	5,689	6,440
Other current assets	2,183	1,510	2,095	2,215	2,507
Investments	1,899	776	776	776	776
Net fixed assets	10,452	11,719	13,601	13,844	14,104
CWIP	613	2,613	1,318	2,000	2,000
Intangible assets	75	67	4,064	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>24,254</b>	<b>26,640</b>	<b>36,400</b>	<b>36,676</b>	<b>42,165</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Net income + Depreciation	5,281	4,589	5,644	5,974	7,180
Interest expenses	4	12	23	52	78
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(2,585)	(186)	(2,515)	(398)	(1,293)
Other operating cash flows	0	0	0	0	0
<b>Cash flow from operations</b>	<b>2,699</b>	<b>4,414</b>	<b>3,152</b>	<b>5,628</b>	<b>5,965</b>
Capital expenditures	(5,224)	(1,930)	(2,500)	(1,302)	(1,393)
Change in investments	(84)	1,123	0	0	0
Other investing cash flows	0	0	0	0	0
<b>Cash flow from investing</b>	<b>(5,307)</b>	<b>(807)</b>	<b>(2,500)</b>	<b>(1,302)</b>	<b>(1,393)</b>
Equities issued/Others	0	(2)	0	0	0
Debt raised/repaid	(55)	330	88	872	0
Interest expenses	(4)	(12)	(23)	(52)	(78)
Dividends paid	(3)	(795)	(882)	(983)	(1,209)
Other financing cash flows	3,040	(3,055)	(3,056)	3,382	0
<b>Cash flow from financing</b>	<b>2,978</b>	<b>(3,533)</b>	<b>(3,874)</b>	<b>3,219</b>	<b>(1,287)</b>
<b>Changes in cash and cash eq.</b>	<b>370</b>	<b>74</b>	<b>(3,222)</b>	<b>7,545</b>	<b>3,284</b>
<b>Closing cash and cash eq.</b>	<b>930</b>	<b>1,004</b>	<b>(2,218)</b>	<b>9,391</b>	<b>8,611</b>

**Per Share**

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20P	FY21E	FY22E
Reported EPS	53.4	44.1	53.3	56.0	68.9
Adjusted EPS	53.4	44.1	50.3	56.0	68.9
Dividend per share	0.0	9.0	10.1	11.2	13.8
Book value per share	235.5	259.1	302.3	347.1	402.3

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19A	FY20P	FY21E	FY22E
EV/Sales	5.9	6.1	4.8	4.5	3.9
EV/EBITDA	19.2	22.2	17.9	16.9	14.4
Adjusted P/E	26.9	32.6	28.6	25.7	20.9
P/BV	6.1	5.6	4.8	4.1	3.6

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19A	FY20P	FY21E	FY22E
Tax burden (Net profit/PBT)	75.3	75.4	69.2	74.0	75.0
Interest burden (PBT/EBIT)	104.0	104.0	105.8	104.9	107.9
EBIT margin (EBIT/Revenue)	28.1	24.0	23.0	22.9	23.8
Asset turnover (Revenue/Avg TA)	29.3	23.5	24.2	22.1	22.9
Leverage (Avg TA/Avg Equity)	1.0	1.0	1.1	1.1	1.0
Adjusted ROAE	25.8	17.8	17.9	17.3	18.4

Source: Company, BOBCAPS Research | Note: TA = Total Assets

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	6.6	(3.6)	27.4	5.7	13.2
EBITDA	(5.9)	(14.1)	23.8	5.6	16.4
Adjusted EPS	(9.8)	(17.4)	14.0	11.4	23.0
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	30.9	27.5	26.7	26.7	27.4
EBIT margin	28.1	24.0	23.0	22.9	23.8
Adjusted profit margin	22.0	18.8	16.8	17.8	19.3
Adjusted ROAE	25.8	17.8	17.9	17.3	18.4
ROCE	34.2	23.5	25.6	22.8	23.8
<b>Working capital days (days)</b>					
Receivables	79	82	108	90	90
Inventory	60	77	69	75	75
Payables	43	40	50	40	40
<b>Ratios (x)</b>					
Gross asset turnover	1.5	1.3	1.4	1.4	1.5
Current ratio	3.1	3.2	3.1	4.1	4.5
Net interest coverage ratio	1,460.1	425.3	261.5	122.1	95.8
Adjusted debt/equity	0.0	0.0	(0.1)	(0.1)	(0.2)

Source: Company, BOBCAPS Research

## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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B – Buy, A – Add, R – Reduce, S – Sell

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