

BUY

TP: Rs 680 | ▲ 15%

ALEMBIC PHARMA

Pharmaceuticals

22 January 2020

Good beat – we raise EPS estimates by 5-7%

Alembic Pharma (ALPM) reported a 15% EBITDA beat in Q3 driven by a sales beat and stable opex despite an additional expense hit from Aleor-Derma unit commercialisation. Solid US sales at US\$ 72mn, healthy ROW revenue and controlled SG&A were key positives. India reported a subdued Q3, but ALPM retained its growth recovery guidance from Q1FY21. Sartan/combination shortages in the US will continue to drive growth over the next 3-6 months. We raise FY21/FY22 EPS by 5-7% led by the Q3 beat. Retain BUY; TP revised to Rs 680.

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US – solid beat; we raise estimates: US sales were 10% ahead of our estimates at US\$ 72mn (-6% QoQ), led by seven launches and stable contribution/pricing from the sartan franchise. Opportunities within sartans should continue for the next 3-6 months at least; ALPM expects 23 launches (17 for 9M) in FY20. We raise US sales estimates by 10% and now expect US\$ 330mn in sales by FY23. We believe ALPM is best placed to participate in the US\$ 20bn worth of LOE (loss of exclusivity) in the next five years (read our Dec'19 [Initiation report](#) for details).

Ticker/Price	ALPM IN/Rs 590
Market cap	US\$ 1.6bn
Shares o/s	189mn
3M ADV	US\$ 1.3mn
52wk high/low	Rs 612/Rs 530
Promoter/FPI/DII	73%/10%/6%

Source: NSE

Key earnings call takeaways: (1) On a like-to-like basis, India business grew 10% YoY in Q3 and margins continued to improve. (2) Q3 gross margin of 75.3% benefitted from sartan shortages but we expect 68-70% margins in the long term. (3) Capex incl. opex capitalised was Rs 1.8bn for Q3 (Rs 5.5bn for 9M incl. Rs 2bn opex capitalised). (4) Net debt as on date stands at Rs 13.5bn.

STOCK PERFORMANCE



Source: NSE

Retain BUY based on doubling of EPS by FY24E, strong FCF: In the next 6-9 months, we believe markets will start to look favourably at ALPM's quality US product lineup (for 2022-26) and with capex turning productive, we see +20% EPS growth visibility over FY21-FY25. ROIC at 23% is higher than large/mid-sized generic players and the strong growth outlook could fuel a rerating. We revise our TP to Rs 680 based on 12x FY22E EV/EBITDA (21x implied P/E).

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	31,310	39,350	43,547	47,304	52,787
EBITDA (Rs mn)	6,711	8,737	10,312	9,950	11,391
Adj. net profit (Rs mn)	4,489	5,928	6,869	6,247	7,223
Adj. EPS (Rs)	23.4	31.0	36.4	33.1	38.3
Adj. EPS growth (%)	11.0	32.4	17.7	(9.1)	15.6
Adj. ROAE (%)	21.0	23.4	22.7	17.5	17.7
Adj. P/E (x)	25.2	19.1	16.2	17.8	15.4
EV/EBITDA (x)	16.3	13.0	11.5	11.9	10.1

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)	Q3FY20E	Var. (%)
Net Sales	12,090	10,182	18.7	12,408	(2.6)	11,576	4.4
EBITDA	3,252	2,422	34.2	3,456	(5.9)	2,821	15.3
Depreciation	418	291	-	359	-	400	-
EBIT	2,834	2,132	32.9	3,097	(8.5)	2,421	-
Interest	74	60	-	70	-	75	-
Other Income	4	35	-	4	-	35	-
PBT	2,764	2,108	31.2	3,031	(8.8)	2,381	16.1
Less: Taxation	485	400	-	525	-	476	-
Less: Minority Interest	(69)	10	-	41	-	40	-
Recurring PAT	2,348	1,698	38.3	2,465	(4.7)	1,865	25.9
Exceptional items	0	0	-	0	-	0	-
Reported PAT	2,348	1,698	38.3	2,465	(4.7)	1,865	25.9
Key Ratios (%)							
Gross Margin	75.3	75.6	-	78.0	-	77.0	-
EBITDA Margin	26.9	23.8	-	27.9	-	24.4	-
Tax / PBT	17.5	19.0	-	17.3	-	20.0	-
NPM	19.4	16.7	-	19.9	-	16.1	-
EPS (Rs)	12.5	9.0	-	13.1	-	9.9	-

Source: Company, BOBCAPS Research

FIG 2 – SEGMENT SALES

(Rs mn)	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)	Q3FY20E	Var. (%)
Formulations	10,320	8,130	26.9	10,370	(0.5)	9,650	6.9
India	3,680	3,650	0.8	3,910	(5.9)	3,760	(2.1)
US	5,150	3,080	67.2	5,390	(4.5)	4,690	9.8
RoW	1,490	1,400	6.4	1,070	39.3	1,200	24.2
API	1,770	2,050	(13.7)	2,040	(13.2)	1,926	(8.1)
Net Sales	12,090	10,180	18.8	12,410	(2.6)	11,576	4.4

Source: Company, BOBCAPS Research

FIG 3 – REGULATORY/COMMERCIALISATION UPDATE ON KEY FACILITIES

Formulation	Dosage form	Audit/Filing Status
Panelav F1	Oral solid	Oct'18*
Panelav F2	Oncology oral solid	June'19*
Panelav F2	Oncology injectable	H2FY21#
Karkhadi F3	Injectable & Ophthalmic	H2FY20#
Jarod F4	Oral solid	H1FY21#
Karkhadi Aleor JV	Dermatology	Jan'20*
API		
Panelav API 1 & 2		Dec'18*
Karkhadi API 3		Jan'20*

Source: Company | #Expected filings, *Last USFDA inspection

Valuation methodology

Mediocre core earnings growth and heavy capex have weighed on ALPM’s share price since 2015. Over the next 6-9 months, we believe markets will start discounting (a) the upcoming sizeable US generic opportunity worth US\$ 20bn (2022-26) and (b) capex turning productive from FY22E. This should support over 20% EPS growth visibility for a relatively prolonged period through to FY25 over the FY21 base earnings.

ALPM’s ROIC of 23% in FY19 is the highest compared to large and midsize generic-focused companies which were at ~15%. Valuations are reasonable at 10x FY22E EV/EBITDA and we believe the stock offers a better risk-reward than peers.

Following the Q3FY20 beat led by the US business, we raise FY21-FY22 EPS estimates by 5-7%. FY20 revision is higher by 14% due to an assumed lower tax rate of 22% (18% for 9MFY20) in addition to the upgrade in US sales.

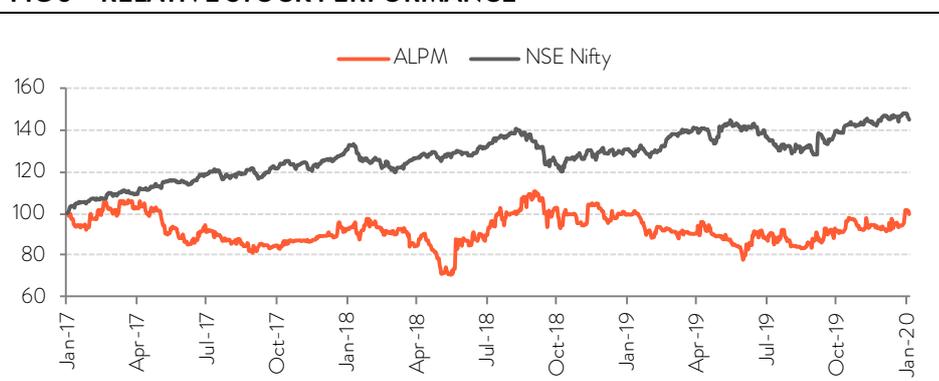
We retain BUY and raise our Mar’21 target price to Rs 680 (from Rs 660), based on an unchanged target EV/EBITDA multiple of 12x on Mar’22E (implied P/E of 21x). We believe the market’s concerns of high US capital allocation and weak margin dynamics are unwarranted and this could drive a large earnings surprise, fuelling a rerating in the stock over the next two years.

FIG 4 – REVISED ESTIMATES

(Rs bn)	New			Old			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Sales	43.5	47.3	52.8	42.6	46.1	51.2	2.3	2.7	3.1
EBITDA	10.3	10.0	11.4	9.4	9.4	10.9	9.4	5.9	4.4
EBITDA margin (%)	23.7	21.0	21.6	22.1	20.4	21.3	154bps	64bps	27bps
EPS (Rs)	36	33	38	32	31	37	13.9	6.9	4.7

Source: Company, BOBCAPS Research

FIG 5 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **US execution critical:** We expect the US market to contribute meaningfully to profitability in the coming years. Any delays with respect to key launches, early generic competition in Theophylline (~12% of FY21E EPS) and tardy commercialisation of the new capacities across Panelav, Karakhadi and Jarod can potentially impact profit growth.
- **US regulatory risk:** A majority of ALPM's US sales are dependent on the Panelav unit (~80% of existing sales). While the compliance track record with the FDA has been clean so far, plant concentration risk remains. We note that ALPM is working towards derisking its current manufacturing concentration to other newer units, but this is still two years away.
- **Regulatory action and slowdown in India formulations business:** Expansion of NLEM (national list of essential medicines) coverage and the FDC (fixed dose combination) ban in 2018 hit growth across the Indian pharmaceutical market. Roughly 15% of ALPM's domestic sales are under price control vs. 17% for the IPM on average. In addition, ALPM has low price leadership in top brands and chronic therapies, which should act as a cushion against substantial risk. However, regulatory action on pricing is unpredictable and hence remains a risk. Further, any slowdown in IPM growth and delays in new launches can adversely affect ALPM's earnings.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue	31,310	39,350	43,547	47,304	52,787
EBITDA	6,711	8,737	10,312	9,950	11,391
Depreciation	1,055	1,152	1,476	1,974	2,392
EBIT	5,656	7,585	8,836	7,976	8,999
Net interest income/(expenses)	(34)	(184)	(301)	(320)	(320)
Other income/(expenses)	70	94	270	563	824
Exceptional items	0	0	0	0	0
EBT	5,692	7,495	8,806	8,219	9,504
Income taxes	1,203	1,567	1,937	1,973	2,281
Extraordinary items	(278)	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	4,211	5,928	6,869	6,247	7,223
Adjustments	(278)	0	0	0	0
Adjusted net profit	4,489	5,928	6,869	6,247	7,223

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	7,593	7,022	8,351	9,072	10,123
Other current liabilities	1,427	1,221	2,177	2,365	2,639
Provisions	751	843	933	1,013	1,131
Debt funds	7,077	11,284	12,784	12,784	12,784
Other liabilities	0	0	0	0	0
Equity capital	377	377	377	377	377
Reserves & surplus	22,177	27,021	32,759	37,686	43,401
Shareholders' fund	22,554	27,398	33,136	38,063	43,778
Total liabilities and equities	39,402	47,768	57,381	63,298	70,455
Cash and cash eq.	898	2,055	6,961	11,818	15,658
Accounts receivables	5,263	4,888	9,545	10,368	13,016
Inventories	7,339	9,672	9,545	10,368	11,570
Other current assets	5,005	3,426	4,355	4,730	5,279
Investments	416	483	483	483	483
Net fixed assets	9,270	10,984	15,233	19,270	20,690
CWIP	10,550	15,660	10,660	5,660	3,160
Intangible assets	661	600	600	600	600
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	39,402	47,768	57,381	63,298	70,455

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	5,185	6,986	8,344	8,221	9,615
Interest expenses	34	184	301	320	320
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(2,308)	(1,064)	(3,082)	(1,034)	(2,955)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	2,911	6,106	5,563	7,507	6,980
Capital expenditures	(2,226)	(2,771)	(5,725)	(6,011)	(3,812)
Change in investments	82	(67)	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(2,144)	(2,838)	(5,725)	(6,011)	(3,812)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	6,192	4,207	1,500	0	0
Interest expenses	(34)	(184)	(301)	(320)	(320)
Dividends paid	(907)	(907)	(1,131)	(1,320)	(1,508)
Other financing cash flows	(6,715)	(5,227)	5,000	5,000	2,500
Cash flow from financing	(1,464)	(2,112)	5,068	3,361	672
Changes in cash and cash eq.	(697)	1,157	4,906	4,857	3,840
Closing cash and cash eq.	898	2,055	6,961	11,818	15,658

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	21.9	31.0	36.4	33.1	38.3
Adjusted EPS	23.4	31.0	36.4	33.1	38.3
Dividend per share	4.0	5.5	6.0	7.0	8.0
Book value per share	119.6	145.3	175.8	201.9	232.2

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	3.5	2.9	2.7	2.5	2.2
EV/EBITDA	16.3	13.0	11.5	11.9	10.1
Adjusted P/E	25.2	19.1	16.2	17.8	15.4
P/BV	4.9	4.1	3.4	2.9	2.5

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	78.9	79.1	78.0	76.0	76.0
Interest burden (PBT/EBIT)	100.6	98.8	99.7	103.1	105.6
EBIT margin (EBIT/Revenue)	18.1	19.3	20.3	16.9	17.0
Asset turnover (Revenue/Avg TA)	31.4	28.8	25.7	24.4	24.6
Leverage (Avg TA/Avg Equity)	1.2	1.4	1.4	1.4	1.3
Adjusted ROAE	21.0	23.4	22.7	17.5	17.7

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

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
YoY growth (%)					
Revenue	(0.1)	25.7	10.7	8.6	11.6
EBITDA	10.1	30.2	18.0	(3.5)	14.5
Adjusted EPS	11.0	32.4	17.7	(9.1)	15.6
Profitability & Return ratios (%)					
EBITDA margin	21.4	22.2	23.7	21.0	21.6
EBIT margin	18.1	19.3	20.3	16.9	17.0
Adjusted profit margin	14.3	15.1	15.8	13.2	13.7
Adjusted ROAE	21.0	23.4	22.7	17.5	17.7
ROCE	22.9	22.5	21.5	17.6	18.3
Working capital days (days)					
Receivables	61	45	80	80	90
Inventory	86	90	80	80	80
Payables	89	65	70	70	70
Ratios (x)					
Gross asset turnover	2.7	2.7	2.2	1.8	1.8
Current ratio	1.9	2.2	2.7	3.0	3.3
Net interest coverage ratio	166.4	41.2	29.4	25.0	28.2
Adjusted debt/equity	0.3	0.3	0.2	0.0	(0.1)

Source: Company, BOBCAPS Research

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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)

HISTORICAL RATINGS AND TARGET PRICE: ALEMBIC PHARMA (ALPM IN)



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

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