

## RESEARCH

### Top picks

- **Mid-cap ideas** – Future Supply replaced by **Transport Corp** (see [Topline disappoints, margin resilient, 30Jan20](#))

### **Alkem Labs** | Target: Rs 2,870 | +15% | **BUY**

Solid beat – moving to street-high TP of Rs 2,870

### **Aurobindo Pharma** | Target: Rs 560 | +10% | **ADD**

Q3 in line; facility resolution, Sandoz key stock catalysts

### **Mphasis** | Target: Rs 1,050 | +11% | **ADD**

Cloudy DXC/HP visibility overshadows strong operating beat

### **Mahanagar Gas** | Target: Rs 950 | –21% | **SELL**

Volumes drag and margins peak out

## SUMMARY

### Alkem Labs

Alkem Labs reported a 24% EBITDA beat in Q3 driven by better gross margins (product mix, soft RM prices). India sales rose 14% YoY; US sales grew 8% QoQ to US\$ 82mn. A focus on strengthening the high-margin India portfolio should drive low double-digit growth in coming years, alongside benefits from US operating leverage. In the mid-term, Alkem expect 20% EBITDA margins (from c.18%). We raise FY21/FY22 EPS by 6%, increase our target EV/EBITDA multiple to 17x vs. 14x leading to Mar'21 TP of Rs 2,870 (implied 24x P/E).

[Click here for the full report.](#)

## TOP PICKS

### LARGE-CAP IDEAS

Company	Rating	Target
<a href="#">Bajaj Finance</a>	Buy	5,200
<a href="#">Cipla</a>	Buy	570
<a href="#">Eicher Motors</a>	Buy	25,000
<a href="#">Petronet LNG</a>	Buy	400
<a href="#">Reliance Industries</a>	Buy	1,860

### MID-CAP IDEAS

Company	Rating	Target
<a href="#">Alkem Labs</a>	Buy	2,870
<a href="#">Greenply Industries</a>	Buy	210
<a href="#">Laurus Labs</a>	Buy	510
<a href="#">Transport Corp</a>	Buy	355
<a href="#">Ashok Leyland</a>	Sell	68

Source: BOBCAPS Research

### DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.64	(1bps)	(17bps)	(102bps)
India 10Y yield (%)	6.45	(6bps)	(12bps)	(87bps)
USD/INR	71.20	0	1.0	0.4
Brent Crude (US\$/bbl)	54.93	(0.6)	(20.3)	(10.9)
Dow	29,380	0.3	2.4	16.7
Shanghai	2,867	1.7	(7.0)	9.5
Sensex	41,306	0.4	1.5	11.7
India FII (US\$ mn)	5 Feb	MTD	CYTD	FYTD
FII-D	311.0	(206.6)	(1,775.5)	1,168.6
FII-E	74.4	462.7	1,835.4	9,224.6

Source: Bank of Baroda Economics Research

### BOBCAPS Research

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## Aurobindo Pharma

Aurobindo's (ARBP) operating results were in line, with above-expected US sales of US\$ 418mn (volume-led) but subdued gross margins at 56.5% (down 120bps QoQ) due to a higher ARV mix. Net debt declined by US\$ 77mn. This coupled with 2-3 months of stock amid potential coronavirus-led supply constraints are other positives. Management expects Sandoz approval latest by Mar'20 and CAPA implementation for Unit 4 by May. Nearing reinspection timelines for Unit 10 and Eugia are other near-term stock catalysts. Retain ADD.

[Click here for the full report.](#)

## Mphasis

Mphasis (MPHL) reported a beat on both revenue and margins in Q3FY20. Upbeat Digital Risk revenues (+14% QoQ CC) aided a strong showing in the Direct core business. However, DXC/HP channel revenue growth was soft at 0.1% QoQ CC. Management continues to target above-industry growth in the direct core business and industry-level growth in DXC/HP for FY20. We tweak FY21/FY22 earnings by +1%/-1% and roll over to a revised Mar'21 TP of Rs 1,050 (vs. Rs 1,020 earlier). Retain ADD.

[Click here for the full report.](#)

## Mahanagar Gas

Mahanagar Gas's (MAHGL) Q3FY20 PAT was in line at Rs 1.86bn (+25.4% YoY). Key Q3 highlights: (a) EBITDA margins disappointed at Rs 9.2/scm (-7% QoQ) on higher costs, and (b) volumes were muted at 281mmscm (+3% YoY). MAHGL lags its peers on volume growth, while its elevated operating margins appear to have peaked out. We marginally trim FY20-FY22 earnings as we cut operating margin estimates to Rs 9.6/scm (from Rs 10), on par with 9MFY20 levels. Our DCF-based TP changes to Rs 950 (vs. Rs 890) on rollover.

[Click here for the full report.](#)

**BUY**

TP: Rs 2,870 | ▲ 15%

**ALKEM LABS**

Pharmaceuticals

07 February 2020

## Solid beat – moving to street-high TP of Rs 2,870

Alkem Labs reported a 24% EBITDA beat in Q3 driven by better gross margins (product mix, soft RM prices). India sales rose 14% YoY; US sales grew 8% QoQ to US\$ 82mn. A focus on strengthening the high-margin India portfolio should drive low double-digit growth in coming years, alongside benefits from US operating leverage. In the mid-term, Alkem expect 20% EBITDA margins (from c.18%). We raise FY21/FY22 EPS by 6%, increase our target EV/EBITDA multiple to 17x vs. 14x leading to Mar'21 TP of Rs 2,870 (implied 24x P/E).

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**24% EBITDA beat, India and US sales steady:** Q3 EBITDA was up 45% YoY led by 450bps expansion in gross margin to 61.8%. EBITDA margins stood at 20.8% vs. our estimate of 17.2%, partially driven by cost control. Q3/9M India sales growth was better than estimates at 14%/15% YoY (in 9M, acute was up 13% and chronic 21%). US commentary is stable with guidance for good growth over FY20 – we expect US\$ 400mn in US sales by FY22 (14% CAGR).

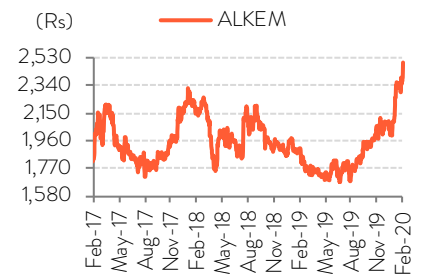
**Scope for rerating; TP raised to Rs 2,870:** We believe Alkem's profitability base has moved up – evident from the beat over the last three quarters, which has led us to cumulatively upgrade EBITDA by 9-10% and margins by 100bps for FY20-FY22. This momentum should sustain given a focus on raising the high-margin acute mix, increasing MR efficiency and driving operating leverage in the US (see our Jul'19 initiation). Coupled with ROIC of >30% from FY21E (vs. ~20% in FY18-FY19) and strong FCF, we expect one-year forward EV/EBITDA multiples to move closer to the 3Y mean of 19x from c.14.8x.

**Earnings call highlights:** (1) Trade margin capping, if implemented, will be therapy-wise. (2) Direct dependency on Chinese API is 5%; stock currently at 1-1.5 months. (3) Expect addition of 300 to the ~11,000 field force in FY21. (4) FY21 capex and tax guided at Rs 4bn and 10% respectively.

Ticker/Price	ALKEM IN/Rs 2,503
Market cap	US\$ 4.2bn
Shares o/s	120mn
3M ADV	US\$ 2.5mn
52wk high/low	Rs 2,558/Rs 1,660
Promoter/FPI/DII	66%/2%/5%

Source: NSE

## STOCK PERFORMANCE



Source: NSE

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	64,218	73,558	82,607	92,525	103,306
EBITDA (Rs mn)	10,284	11,135	14,255	16,779	19,480
Adj. net profit (Rs mn)	6,309	7,298	11,238	13,387	14,392
Adj. EPS (Rs)	52.8	61.0	94.0	112.0	120.4
Adj. EPS growth (%)	(29.3)	15.7	54.0	19.1	7.5
Adj. ROAE (%)	15.8	16.3	21.8	21.9	20.1
Adj. P/E (x)	47.4	41.0	26.6	22.3	20.8
EV/EBITDA (x)	28.9	26.9	21.1	17.6	14.8

Source: Company, BOBCAPS Research



**ADD**

TP: Rs 560 | ▲ 10%

**AUROBINDO PHARMA**

Pharmaceuticals

07 February 2020

### Q3 in line; facility resolution, Sandoz key stock catalysts

Aurobindo's (ARBP) operating results were in line, with above-expected US sales of US\$ 418mn (volume-led) but subdued gross margins at 56.5% (down 120bps QoQ) due to a higher ARV mix. Net debt declined by US\$ 77mn. This coupled with 2-3 months of stock amid potential coronavirus-led supply constraints are other positives. Management expects Sandoz approval latest by Mar'20 and CAPA implementation for Unit 4 by May. Nearing reinspection timelines for Unit 10 and Eugia are other near-term stock catalysts. Retain ADD.

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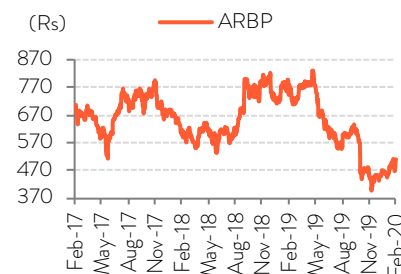
**US beat key positive but EBITDA in line:** ARBP saw best-ever US sales of US\$ 418mn in Q3 (+3% QoQ), led by new launches and volume growth in the base portfolio. Management believes the NBO opportunity might continue. Going ahead, Eugia will start contributing significantly in FY21 (currently only two products from this site). 9M US sales are tracking ahead of estimates, driving a 5% EPS upgrades for FY21/FY22. Spectrum's annualised sales of US\$ 100mn are tracking slightly above estimates. Injectable sales were flat QoQ at US\$ 76mn in Q3. EBITDA margin of 20.5% was in line. ARBP aims to be debt-free (outstanding net debt US\$ 446mn) in three years.

Ticker/Price	ARBP IN/Rs 511
Market cap	US\$ 4.2bn
Shares o/s	586mn
3M ADV	US\$ 23.8mn
52wk high/low	Rs 838/Rs 389
Promoter/FPI/DII	52%/19%/15%

Source: NSE

**Near-term events to watch:** While a final say on Unit 4 (injectable unit & ~5% of FY21E sales) is awaited, we believe Unit 10 and Eugia (together 55 pending ANDAs accounting for 42% of pending files) will come up for inspection in the next 3-4 months. Both units will be key growth drivers over the next 2-3 years.

### STOCK PERFORMANCE



Source: NSE

**ADD:** Strong US sales despite facility challenges is a key positive in Q3. But stock valuations have turned reasonable from attractive post a 35% rally (trading at 8x FY21E EBITDA, 10% premium to peers). We revise Mar'21 TP to Rs 560 (from Rs 500), based on ~7x EV/EBITDA. Downside risks: Unit 4 escalation, Sandoz consolidation delays, penalty risk from Aceto supply sabotage claim.

### KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	164,630	195,634	230,854	285,827	292,957
EBITDA (Rs mn)	37,718	39,519	47,118	55,500	57,116
Adj. net profit (Rs mn)	24,227	24,126	27,331	28,939	29,294
Adj. EPS (Rs)	41.3	41.2	46.6	49.4	50.0
Adj. EPS growth (%)	5.3	(0.4)	13.3	5.9	1.2
Adj. ROAE (%)	23.1	18.8	18.0	16.4	14.4
Adj. P/E (x)	12.3	12.4	10.9	10.3	10.2
EV/EBITDA (x)	8.9	8.4	7.3	6.2	6.5

Source: Company, BOBCAPS Research



**ADD**

TP: Rs 1,050 | ▲ 11%

**MPHASIS**

| IT Services

| 07 February 2020

## Cloudy DXC/HP visibility overshadows strong operating beat

Mphasis (MPHL) reported a beat on both revenue and margins in Q3FY20. Upbeat Digital Risk revenues (+14% QoQ CC) aided a strong showing in the Direct core business. However, DXC/HP channel revenue growth was soft at 0.1% QoQ CC. Management continues to target above-industry growth in the direct core business and industry-level growth in DXC/HP for FY20. We tweak FY21/FY22 earnings by +1%/–1% and roll over to a revised Mar’21 TP of Rs 1,050 (vs. Rs 1,020 earlier). Retain ADD.

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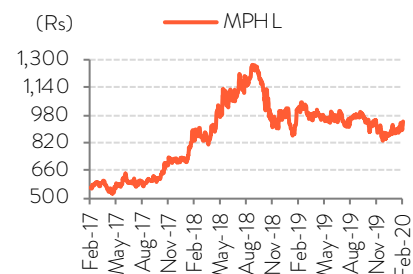
**Digital Risk uplifts Q3 performance:** MPHL reported an operational beat in Q3 as revenue grew 4% QoQ CC (~2% est.), aided by 4.5% QoQ CC growth in the direct core business. The Digital Risk business grew 14% QoQ CC (partly led by favourable dynamics for the US mortgage market in the Dec’19 quarter), supporting the strong showing in the direct core business. In contrast, DXC/HP channel performance was subdued, with 0.1% QoQ CC revenue growth.

Ticker/Price	MPHL IN/Rs 943
Market cap	US\$ 2.5bn
Shares o/s	186mn
3M ADV	US\$ 2.6mn
52wk high/low	Rs 1,063/Rs 828
Promoter/FPI/DII	52%/29%/14%

Source: NSE

**Resilient operating margins:** EBIT margin at 16.2% (15.6% est.) was up 10bps QoQ despite annual wage hike headwinds. Annual wage revision will continue to have a lower impact than historical trends as the company has moved to a new deferred wage revision policy in FY20 (aligned with reskilling).

## STOCK PERFORMANCE



Source: NSE

**Cloudy DXC/HP business visibility:** The DXC/HP channel (26.6% of Q3 revenue) has posted tepid growth over the last two quarters, largely due to a sequential decline in non-DXC business (refer Fig 2 & 3). The change of guard at DXC in Sep’19 and subsequent strategy refresh further raises risks for MPHL, given that DXC accounts for a large portion of channel revenue (62% in Q3). MPHL’s management sees little impact, citing a status quo on the relationship, and has maintained guidance of above-industry growth in direct core business, industry-level growth in DXC/HP and 15.5-17% EBIT margins for FY20.

## KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	65,459	77,311	88,042	99,612	1,10,610
EBITDA (Rs mn)	10,626	13,240	16,268	18,810	20,761
Adj. net profit (Rs mn)	8,507	10,734	11,225	12,414	13,982
Adj. EPS (Rs)	44.1	57.7	60.3	66.7	75.1
Adj. EPS growth (%)	14.9	30.9	4.6	10.6	12.6
Adj. ROAE (%)	14.6	20.0	20.4	20.5	21.0
Adj. P/E (x)	21.4	16.4	15.6	14.1	12.6
EV/EBITDA (x)	16.2	13.1	10.7	9.3	8.4

Source: Company, BOBCAPS Research



**SELL**  
 TP: Rs 950 | ▼ 21%

**MAHANAGAR GAS**

Oil & Gas

07 February 2020

### Volumes drag and margins peak out

Mahanagar Gas’s (MAHGL) Q3FY20 PAT was in line at Rs 1.86bn (+25.4% YoY). Key Q3 highlights: (a) EBITDA margins disappointed at Rs 9.2/scm (-7% QoQ) on higher costs, and (b) volumes were muted at 281mmscm (+3% YoY). MAHGL lags its peers on volume growth, while its elevated operating margins appear to have peaked out. We marginally trim FY20-FY22 earnings as we cut operating margin estimates to Rs 9.6/scm (from Rs 10), on par with 9MFY20 levels. Our DCF-based TP changes to Rs 950 (vs. Rs 890) on rollover.

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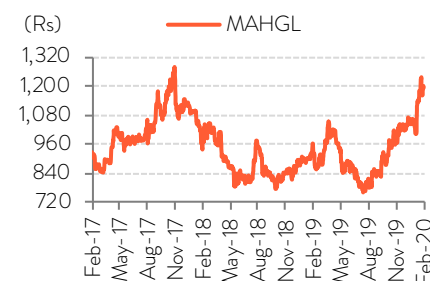
**Muted volume growth:** MAHGL’s volume growth continues to be subpar when compared to its CGD peers, at 3% YoY in Q3 (281mmscm). CNG growth (205mmscm, +2.4% YoY) was muted due to a high base and slowdown in the addition or conversion rate of vehicles using this fuel. The downturn in CNG volume growth could continue over the long term given rising infrastructure constraints and improving alternate travel options in Mumbai (metro). We maintain volume growth estimates at 3.5% CAGR over FY20-FY22, lagging peers (Indraprastha Gas and Gujarat Gas) that offer >10% CAGR.

Ticker/Price	MAHGL IN/Rs 1,199
Market cap	US\$ 1.7bn
Shares o/s	99mn
3M ADV	US\$ 13.4mn
52wk high/low	Rs 1,246/Rs 754
Promoter/FPI/DII	33%/32%/36%

Source: NSE

**Margins have peaked – as expected:** EBITDA margins for Q3 were below estimates at Rs 9.2/scm (-7% QoQ). Among GAIL-owned CGD companies, MAHGL continues to have one of the highest operating margins, but one of the lowest volume growth rates. We see a high probability for margins to decline further as the company could choose to chase volumes.

### STOCK PERFORMANCE



Source: NSE

**Maintain SELL:** We raise our DCF-based TP for MAHGL to Rs 950 on rollover to Mar’21. At 14.3x FY22E EPS, the stock continues to attract among the lowest multiples, but valuations look justified on stagnant earnings growth. Margins have peaked out and we now estimate EBITDA/scm at ~Rs 9.6 (FY20-FY22).

### KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	22,330	27,911	33,250	36,329	39,201
EBITDA (Rs mn)	7,801	8,855	10,880	11,382	11,852
Adj. net profit (Rs mn)	4,780	5,467	8,194	8,007	8,298
Adj. EPS (Rs)	48.4	55.3	83.0	81.1	84.0
Adj. EPS growth (%)	21.5	14.4	49.9	(2.3)	3.6
Adj. ROAE (%)	24.3	24.2	31.8	27.6	25.6
Adj. P/E (x)	24.8	21.7	14.4	14.8	14.3
EV/EBITDA (x)	15.0	13.2	10.7	10.1	9.5

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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