FIRST LIGHT

14 November 2022

RESEARCH

HERO MOTOCORP | TARGET: Rs 2,712 | +2% | HOLD

Efforts on to capture premium market

ALKEM LABS | TARGET: Rs 2,700 | –15% | SELL

Near-term outlook weak – cut to SELL

LUPIN | TARGET: Rs 700 | –3% | HOLD

Return to double-digit margins

BOB ECONOMICS RESEARCH | IIP

IIP growth scales up

ASTRAL | TARGET: Rs 2,205 | +7% | HOLD

Inventory loss, one-off expenses drag margin

Daily macro indicators

Indicator	09-Nov	10-Nov	Chg (%)
US 10Y yield (%)	4.09	3.81	(28bps)
India 10Y yield (%)	7.39	7.35	(4bps)
USD/INR	81.43	81.81	(0.5)
Brent Crude (US$/bbl)	92.7	93.7	1.1
Dow	32,514	33,715	3.7
Hang Seng	16,359	16,081	(1.7)
Sensex	61,034	60,614	(0.7)
India FII (US$ mn)	**07-Nov**	**09-Nov**	**Chg ($ mn)**
FII-D	(45.6)	33.9	79.5
FII-E	236.2	67.1	(169.2)

Source: Bank of Baroda Economics Research

SUMMARY

HERO MOTOCORP

- Q2 revenue grew 7% YoY backed by realisation gains of 8%, which offset flat volumes on a weak base
- Gross margin was flat YoY at 28% as raw material cost remained high (but stabilised QoQ at 72% of sales)
- We assume coverage with HOLD given limited upside triggers; TP at Rs 2,712

Click here **for the full report.**

ALKEM LABS

- Revenue grew 10% YoY to Rs 31bn in Q2 led by India business, but US price erosion continued to weigh on margins
- Margin guidance pared given US market challenges, though cost initiatives could save Rs 2bn-2.5bn over 12M
- We cut FY23/FY24 EBITDA 12%/18% and our TP to Rs 2,700 (vs. Rs 3,220); downgrade from HOLD to SELL

Click here **for the full report.**

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LUPIN

- Q2 revenue grew 11% QoQ (+1% YoY) with recovery in US business and continued momentum in India
- EBITDA margin returned to double digits (10.5%), rising 610bps QoQ; gross margin rose 170bps
- We adjust FY23/FY24 EBITDA -8%/+5% and raise our target EV/EBITDA to 11x, yielding a new TP of Rs 700 (vs. Rs 600); upgrade to HOLD

Click here for the full report.

INDIA ECONOMICS: IIP

Industrial growth increased by 3.1% in Sep'22 (-0.7% in Aug'22). Higher output is on the back of growth in electricity output which was up by 11.6% in Sep'22 and mining output growing by 4.6% from a contraction of 3.9% in Aug'22. Manufacturing output (77.6%) which contributes the most to the industrial production was up a tad bit by 1.8% in Sep'22 (-0.5% in Sep'22). Even as fears of global economic slowdown aggravate across countries. India's growth remain steady with industrial production output likely to improve H2FY23 on the back of steady recovery as has also been signalled by some frequency indicators (robust tax collections, soaring credit growth).

Click here for the full report.

ASTRAL

- Consolidated Q2 revenue declined 2% YoY with plumbing down 11% but paints & adhesives up 27%; pipe volumes dipped 4%
- Operating margin contracted 535bps YoY to 12.3% due to inventory loss, high employee cost and expenses toward new products
- Retain TP of Rs 2,205 (set at 62x FY24E EPS) – retain HOLD.

Click here for the full report.

HOLD
TP: Rs 2,712 | ⮝ 2%

HERO MOTOCORP | Automobiles | 11 November 2022

Efforts on to capture premium market

- **Q2 revenue grew 7% YoY backed by realisation gains of 8%, which offset flat volumes on a weak base**
- **Gross margin was flat YoY at 28% as raw material cost remained high (but stabilised QoQ at 72% of sales)**
- **We assume coverage with HOLD given limited upside triggers; TP at Rs 2,712**

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Revenue driven by higher ASP: HMCL reported Q2FY23 revenue growth of 7% YoY to Rs 90.8bn purely driven by a higher average selling price (ASP: Rs 63.5k, +8% YoY/+7% QoQ) on the back of an improved mix and price hikes. Volume growth was flat YoY and remains a concern. Raw material cost remained elevated, keeping gross margin flat YoY at 28%, but higher other expenses pulled EBITDA margin down to 11.4% (-120bps YoY) with EBITDA declining 3% YoY to Rs 10.4bn. This translated into a 10% YoY drop in PAT to Rs 7.2bn.

Demand push beyond pent-up volumes remains key: Q2 volumes grew % QoQ and retail sales climbed even higher by 20% due to pent-up demand post-Covid. While the revival in rural sentiment should be helpful, we believe HMCL will find it challenging to sustain volume growth. We pencil in a 9% uptick for each of the next two years.

Focus on premiumisation with launch of high-end models: Management indicated that it is focused on regaining lost market share in the 125cc+ segment. This will be through launches of 'X-Tec' variants in all key models, new model introductions in the premium space over the next 4-6 quarters, and product rollouts under its Harley Davidson tie-up.

Softening of key input costs to provide relief: Management indicated that metal prices are softening, which translated into relief of 30-40bps QoQ in raw material cost as a percentage of sales. Efforts to improve efficiencies and the easing of supply chain disruptions should be margin-accretive, though rupee depreciation and the energy cost spike are now key headwinds. HMCL did not proffer any margin guidance.

HOLD, TP Rs 2,712: We model for a revenue/EBITDA/adj. PAT CAGR of 9%/7%/2% over FY20-FY25, with EBITDA margin averaging at ~13%. Our FY23/FY24/FY25 EPS estimates stand at Rs 133/Rs 174/Rs 200, 10% lower than consensus on average as we build in softer gross margin assumptions. Valuing HMCL at 15x FY24E EPS – in line with its 10Y mean – and including Rs 100 as the value for other business, we arrive at an SOTP-based TP of Rs 2,712. We see limited upside triggers and hence recommend HOLD.

Key changes

Target	Rating
▼	▼

Ticker/Price	HMCL IN/Rs 2,669
Market cap	US$ 6.6bn
Free float	65%
3M ADV	US$ 20.9mn
52wk high/low	Rs 2,939/Rs 2,147
Promoter/FPI/DII	35%/30%/24%

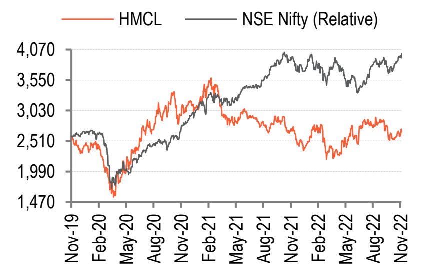
Source: NSE | Price as of 11 Nov 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	292,455	331,054	382,719
EBITDA (Rs mn)	33,688	37,778	48,969
Adj. net profit (Rs mn)	24,730	26,498	34,778
Adj. EPS (Rs)	123.8	132.7	174.2
Consensus EPS (Rs)	123.8	151.5	186.0
Adj. ROAE (%)	15.7	16.0	19.2
Adj. P/E (x)	21.5	20.1	15.3
EV/EBITDA (x)	15.7	14.1	10.9
Adj. EPS growth (%)	(16.6)	7.1	31.2

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

SELL

TP: Rs 2,700 | ∀ 15%

ALKEM LABS | Pharmaceuticals | 14 November 2022

Near-term outlook weak – cut to SELL

- **Revenue grew 10% YoY to Rs 31bn in Q2 led by India business, but US price erosion continued to weigh on margins**
- **Margin guidance pared given US market challenges, though cost initiatives could save Rs 2bn-2.5bn over 12M**
- **We cut FY23/FY24 EBITDA 12%/18% and our TP to Rs 2,700 (vs. Rs 3,220); downgrade from HOLD to SELL**

Saad Shaikh
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India business fuels growth led by acute therapies: Alkem reported 10% YoY revenue growth in Q2FY23 to Rs 30.8bn. India sales climbed 13%, outperforming the domestic market (+8%), led by price hikes, launches and volume gains. The company did well in acute therapies such as anti-infectives (+8% YoY), gastrointestinal (+23%), vitamins, minerals & nutrients (VMN: +12%), and pain management (+19%). Both anti-infectives and VMN were up against a high Covid-led base of last year. Anti-diabetes revenue in the chronic space grew 30% YoY led by launches such as Sitagliptin. The acute/chronic mix stood at 84%/16%.

Persistent challenges in US market: US business clocked in at US$ 74mn in Q2 (+5.5% QoQ constant currency), but continued to face substantial pricing pressure, which depleted both gross (-470bps YoY to 57.6%) and EBITDA margins (-760bps YoY to 14.7%). Management intends to hold back capital allocation for the US market in light of the challenges to growth.

Margin guidance cut: Management has reduced its guided EBITDA margin range by ~100bps to 15-15.5% for FY23 (11.6% reported in H1). This is entirely attributed to the US business as Alkem expects healthy domestic margins where higher raw material prices are likely to be offset by a better product mix. To promote margin expansion, the company is undertaking cost-saving initiatives in areas such as network optimisation and restructuring. Management estimates savings of Rs 2bn-2.5bn from these measures over the next 12 months.

Downgrade to SELL: Relentless price erosion in the US market and elevated input cost, along with higher marketing spends, continue to take a toll on margins. We expect sluggish US business as investments are recalibrated amid challenges to growth. Further, baking in the softer margin guidance, we cut our FY23/FY24 EBITDA estimates by 12%/18%. Our TP consequently reduces to Rs 2,700 (vs. Rs 3,220), based on an unchanged 15x FY24E EV/EBITDA – a discount of 15% to the stock's 5Y average. Given 15% downside potential from the current stock price, we downgrade our rating from HOLD to SELL.

Key changes

Target	Rating
▼	▼

Ticker/Price	ALKEM IN/Rs 3,173
Market cap	US$ 4.7bn
Free float	39%
3M ADV	US$ 4.3mn
52wk high/low	Rs 3,786/Rs 2,828
Promoter/FPI/DII	59%/5%/14%

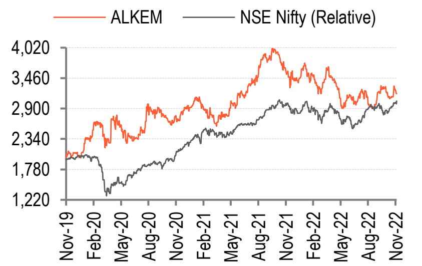
Source: NSE | Price as of 11 Nov 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	1,06,342	1,18,315	1,32,831
EBITDA (Rs mn)	20,529	17,490	20,825
Adj. net profit (Rs mn)	16,606	12,988	15,782
Adj. EPS (Rs)	138.9	108.6	132.0
Consensus EPS (Rs)	138.9	117.0	149.4
Adj. ROAE (%)	24.4	16.7	17.9
Adj. P/E (x)	22.8	29.2	24.0
EV/EBITDA (x)	18.5	21.5	18.0
Adj. EPS growth (%)	4.8	(21.8)	21.5

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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HOLD
TP: Rs 700 | ⮟ 3%

LUPIN | Pharmaceuticals | 11 November 2022

Return to double-digit margins

- **Q2 revenue grew 11% QoQ (+1% YoY) with recovery in US business and continued momentum in India**
- **EBITDA margin returned to double digits (10.5%), rising 610bps QoQ; gross margin rose 170bps**
- **We adjust FY23/FY24 EBITDA -8%/+5% and raise our target EV/EBITDA to 11x, yielding a new TP of Rs 700 (vs. Rs 600); upgrade to HOLD**

Saad Shaikh
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Recovery in US business drives sequential growth: LPC reported sequential revenue growth of 11% to Rs 41.5bn (flat YoY) in Q2FY23, primarily on account of a bounce-back in US business. US revenue grew 31% QoQ to US$ 159mn supported by higher contribution from the complex and respiratory franchise, optimisation of oral solid dosage forms and new product launches including gSuprep. Contribution from respiratory products increased with market share gains in Albuterol Sulfate (to 21.3%).

India growth muted: LPC's India growth was subdued at 6% QoQ (+3% YoY) due to loss of exclusivity in the diabetes (genericisation of gliptins) and cardiovascular therapy areas. Therapies such as cardiac, gastrointestinal, anti-tuberculosis and gynaecology registered double-digit growth YoY. The company launched six brands in Q2FY23. Also, management expects growth momentum in India to accelerate given field force expansion by 850 market representatives (~15% of the existing force) by the year end.

EBITDA margin guided at 16-17%: EBITDA margin regained double-digit territory at 10.5% (+610bps QoQ) after three weak quarters, backed by sequential improvement in gross margin and cost optimisation measures. Gross margin rose 170bps QoQ to 58.7% (-155bps YoY) on the back of higher sequential sales, limited US price erosion (single-digit), a better product mix, benefits from cost control and the presence of a one-time shelf stock adjustment in the previous quarter.

Margins were further aided by a higher contribution from the respiratory franchise and new products. Management has guided for a 16-17% EBITDA margin in FY23 aided by continued cost discipline and significant launches such as gSpiriva.

Upgrade to HOLD: We have a new TP of Rs 700 (vs. Rs 600) as we adjust FY23/ FY24 EBITDA estimates by -8%/+5% to bake in the H1FY23 margin trend and raise our target FY24E EV/EBITDA multiple to 11x (implied 22x P/E) from 10x as LPC is rebounding from three quarters of weak margins. Our multiple is at 10% discount to the stock's 1Y forward EV/EBITDA considering continued regulatory impediments and near-term operational and industry challenges; upgrade from SELL to HOLD.

Key changes

Target	Rating
▲	▲

Ticker/Price	LPC IN/Rs 719
Market cap	US$ 4.0bn
Free float	53%
3M ADV	US$ 11.7mn
52wk high/low	Rs 972/Rs 583
Promoter/FPI/DII	47%/16%/24%

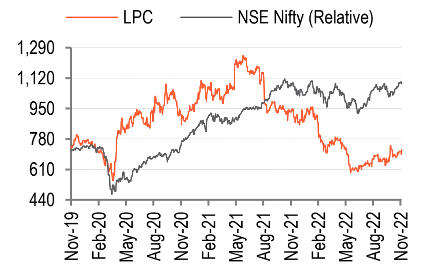
Source: NSE | Price as of 10 Nov 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	1,64,056	1,64,389	1,85,588
EBITDA (Rs mn)	21,657	20,257	30,543
Adj. net profit (Rs mn)	10,581	7,615	14,580
Adj. EPS (Rs)	23.4	16.8	32.2
Consensus EPS (Rs)	23.4	17.6	33.1
Adj. ROAE (%)	8.1	6.1	11.1
Adj. P/E (x)	30.8	42.7	22.3
EV/EBITDA (x)	14.7	16.3	11.3
Adj. EPS growth (%)	(13.0)	(28.0)	91.5

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

IIP

11 November 2022

IIP growth scales up

Aditi Gupta
Economist

Industrial growth increased by 3.1% in Sep'22 (-0.7% in Aug'22). Higher output is on the back of growth in electricity output which was up by 11.6% in Sep'22 and mining output growing by 4.6% from a contraction of 3.9% in Aug'22. Manufacturing output (77.6%) which contributes the most to the industrial production was up a tad bit by 1.8% in Sep'22 (-0.5% in Sep'22). Even as fears of global economic slowdown aggravate across countries. India's growth remain steady with industrial production output likely to improve H2FY23 on the back of steady recovery as has also been signalled by some frequency indicators (robust tax collections, soaring credit growth).

IIP growth moves up:

As against our expectations (4.7%), industrial output rose to 3.1% in Sep'22 after declining by 0.7% in Aug'22. This was led by improvement in electricity (11.6% from 1.4%) and mining (4.6% after contracting by 3.9% in Aug'22) output. Manufacturing output inched up marginally by 1.8% in Sep'22 compared with contraction of 0.5% in Aug'22. Within manufacturing, output improved the most in case of tobacco products, fabricated metal (2.9% versus -7.3%), motor vehicles (29.9% from 23.7%), paper (6.5% versus 0.4%) and food products. Output of electrical equipment and wearing apparel contracted further in Sep'22 from Aug'22. Compared with the levels seen in 2019 (pre-pandemic period), IIP growth was up by 8.6% in Sep'22 versus 4.2% in Aug'22.

Primary good shines:

Within use-based, primary good output accelerated by 9.3% in Sep'22 compared with a growth of 1.7% in Aug'22. Capital goods output clocked double digit growth and was up by 10.3% in Sep'22 (from 4.3% in Aug'22). Infra (7.4% from 2.1% in Aug'22) and intermediate good (2% from 1.2% in Aug'22) output also registered an improvement in Sep'22. However, output of consumer durable disappointed the most as it contracted by 4.5% against a decline of 2.5% in Aug'22. Output of consumer non-durable goods contracted at a slower pace by 7.1% in Sep'22 (-9.5% in Aug'22).

H2FY23 holds key to growth:

In H1FY23, IIP growth has expanded by 7% compared with 23.8% growth in H1FY22. Recently, India's manufacturing PMI had slipped slightly to 55.1 in Sep'22 from 56.2 in Aug'22, though it moved up to 55.3 in Oct'22. The latter half of the year is likely to do much better on the back of the favorable base and taking in to account the festive demand, in this period. Robust tax collections, likelihood of moderation in inflation and uptick in government spending in the coming months is expected to boost the economy.

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HOLD
TP: Rs 2,205 | ⮝ 7%

ASTRAL | Plastic Products | 11 November 2022

Inventory loss, one-off expenses drag margin

- **Consolidated Q2 revenue declined 2% YoY with plumbing down 11% but paints & adhesives up 27%; pipe volumes dipped 4%**
- **Operating margin contracted 535bps YoY to 12.3% due to inventory loss, high employee cost and expenses toward new products**
- **Retain TP of Rs 2,205 (set at 62x FY24E EPS) – retain HOLD.**

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Revenue declines: ASTRA's consolidated Q2FY23 revenue dipped 2% YoY to Rs 11.7bn, as the plumbing business declined 11% due to a substantial fall in PVC prices whereas paints & adhesives grew 27% (includes Gem Paints). The company also lost six working days due to the merger of Resinova Chemie. Standalone revenue declined 7% YoY with EBITDA margin contraction of 520bps YoY to 12.5% due to a 4% drop in pipe volumes given higher destocking by channel partners. For H1, volumes grew 15%.

Margin contracts: Consolidated EBITDA margin contracted 535bps YoY to 12.3% due to one-offs from high-cost inventory (loss of ~Rs 450mn), elevated A&P spends, high employee cost (+140bps) and expenses toward a foreign trip arranged for channel partner. EBIT margin in plumbing fell 540bps YoY to 10% owing to a decline in PVC prices to the tune of Rs 30/kg. The paints & adhesives segment improved its EBIT margin by 125bps to 7% aided by Gem Paints business (unlike in Q2FY22).

Better placed than peers: Due to a better value-added product mix and higher CPVC contribution, ASTRA's EBIT margin in plumbing was at 10%. In contrast, SI's EBIT margin in plastic pipes was just 1.9% and FNXP reported negative EBIT.

EBITDA/kg to revive in Q4: ASTRA incurred an inventory loss of ~Rs 450mn in Q2 and ~Rs 250mn in Q1 due to falling PVC prices. This pulled down EBITDA/kg to Rs 32.1 vs. Rs 44.9 in Q2FY22 and Rs 36.2 in Q1FY23. PVC prices declined by Rs 30/kg during Q2 and channel partners are maintaining lean inventory. However, most of the company's high-cost inventory has been absorbed in H1. Management expects a limited fall in EBITDA/kg in Q3 and revival in Q4.

Maintain HOLD: We like ASTRA for its strong growth prospects, market leadership, net debt-free balance sheet, wide distribution with strong retail franchise, and healthy return ratios. The stock is trading at 58x FY24E EPS. Our TP remains at Rs 2,205, set at 62x FY24E EPS (vs. the 5Y median of ~73x), which offers limited 7% upside potential – retain HOLD.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	ASTRA IN/Rs 2,062
Market cap	US$ 5.1bn
Free float	44%
3M ADV	US$ 14.6mn
52wk high/low	Rs 2,655/Rs 1,582
Promoter/FPI/DII	56%/16%/28%

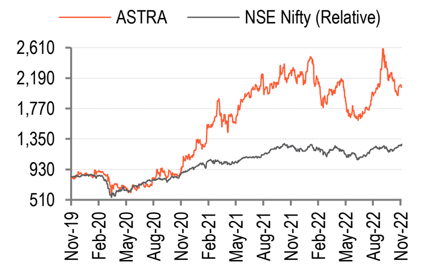
Source: NSE | Price as of 11 Nov 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	43,940	52,095	59,596
EBITDA (Rs mn)	7,553	9,159	10,781
Adj. net profit (Rs mn)	4,906	5,839	7,141
Adj. EPS (Rs)	24.4	29.1	35.5
Consensus EPS (Rs)	24.4	27.3	35.4
Adj. ROAE (%)	23.2	22.5	22.7
Adj. P/E (x)	84.4	70.9	58.0
EV/EBITDA (x)	54.6	44.7	37.7
Adj. EPS growth (%)	20.9	19.0	22.3

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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