FIRST LIGHT

22 May 2023

RESEARCH

SIEMENS INDIA | TARGET: Rs 3,700 | –1% | HOLD

Low-voltage deal appears unfavourable; cut to HOLD

BOB ECONOMICS RESEARCH | CURRENCY OUTLOOK

INR under pressure

ITC | TARGET: Rs 486 | +16% | BUY

Strong performance amid macro headwinds

STATE BANK OF INDIA | TARGET: Rs 729 | +27% | BUY

Sustaining growth and profitability

SYRMA SGS | TARGET: Rs 440 | +34% | BUY

Strong show; positive outlook intact

THE RAMCO CEMENTS | TARGET: Rs 585 | –31% | SELL

Strong volume push but pricing pressure persists

ALKEM LABS | TARGET: Rs 3,000 | –9% | SELL

Margin improvement key for revival

Daily macro indicators

Ticker	17-May	18-May	Chg (%)
US 10Y yield (%)	3.56	3.65	8bps
India 10Y yield (%)	6.97	6.99	2bps
USD/INR	82.39	82.59	(0.2)
Brent Crude (US$/bbl)	77.0	75.9	(1.4)
Dow	33,421	33,536	0.3
Hang Seng	19,561	19,727	0.9
Sensex	61,561	61,432	(0.2)
India FII (US$ mn)	**16-May**	**17-May**	**Chg ($ mn)**
FII-D	141.3	182.5	41.3
FII-E	208.6	97.8	(110.7)

Source: Bank of Baroda Economics Research

SUMMARY

SIEMENS INDIA

- Low-voltage and geared motors business divested to parent for Rs 22bn (2.1x revenue)
- Management expects remaining divisions to offset loss of business on account of the hive-off)
- We find deal valuations unfavourable; cut to HOLD with a revised TP of Rs 3,700 (vs. Rs 4,500) on a lower 52x target P/E (vs. 62x)

Click here **for the full report.**

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INDIA ECONOMICS: CURRENCY OUTLOOK

After remaining stable for most part of the last few months, INR has come under pressure in the last few sessions. In May'23, INR has depreciated by 0.9%. However, bulk of the weakness in INR can be traced back to the last couple of sessions. In fact, since 12 May 2023 (when INR was last below the 82/$ mark), INR has depreciated by 0.6%. Prior to this, INR was fairly steady in a narrow range of 81.5-82/$. This was underpinned by robust macro fundamentals, improvement in external position, lower oil prices and buoyancy in FPI inflows.

Click here **for the full report.**

ITC

- Growth momentum continues with 330bps YoY EBITDA margin expansion; we expect 12% topline growth in FY24
- FMCG business sustains healthy double-digit growth momentum at 19% YoY with steady margin improvement
- Continued investment in capacity and strong execution to drive growth; maintain BUY with a higher TP of Rs 486 (earlier Rs 459)

Click here **for the full report.**

STATE BANK OF INDIA

- Lower provisioning supported robust 83% YoY PAT growth in Q4, though PPOP declined sequentially on higher opex
- Deposit repricing had no major impact on NIM (guided to hold at 3%); recovery in other income likely offset elevated opex
- We assume coverage with BUY and a TP of Rs 729 (1.3x FY25E ABV)

Click here **for the full report.**

SYRMA SGS

- Q4 topline/PAT up 83%/160% YoY spurred by strong growth in the auto and consumer segments
- FY24 revenue growth guidance of 35-40% intact, backed by Rs 30bn order book; 8-10 key clients added in H2FY23
- Maintain BUY with a revised TP of Rs 440 (vs. Rs 400) on rollover

Click here **for the full report.**

THE RAMCO CEMENTS

- New capacities (+2mt YoY) aided 45% jump in Q4 volumes (28% net of added capacities)
- Margin gains QoQ driven by softening of fuel cost from Rs 2.4/kcal to Rs 2.2; YoY cost remains elevated
- FY24/FY25 EPS raised 21%/8% on volume gains, yielding a revised TP of Rs 585 (vs. Rs 534); retain SELL on expensive valuations

Click here for the full report.

ALKEM LABS

- Q4 EBITDA/PAT of Rs 3.5bn/Rs 710mn well short of consensus by 21%/ 79% primarily due to higher operating costs
- Increased sales and marketing spend, field force addition and US price erosion ate into margins
- Insipid US sales remain a challenge; maintain SELL with an unchanged TP of Rs 3,000

Click here for the full report.

COMPANY UPDATE

BOBCAPS
TRUST | INNOVATION | EXCELLENCE

HOLD

TP: Rs 3,700 | ▼ 1%

SIEMENS INDIA | Capital Goods | 19 May 2023

Low-voltage deal appears unfavourable; cut to HOLD

- **Low-voltage and geared motors business divested to parent for Rs 22bn (2.1x revenue)**
- **Management expects remaining divisions to offset loss of business on account of the hive-off)**
- **We find deal valuations unfavourable; cut to HOLD with a revised TP of Rs 3,700 (vs. Rs 4,500) on a lower 52x target P/E (vs. 62x)**

Vinod Chari | Swati Jhunjhunwala
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LV business sold for Rs 22bn: SIEM is selling its low-voltage (LV) and geared motors business to parent Siemens AG for a consideration of Rs 22bn. The business has been valued at Rs 20.7bn-21.65bn by an independent valuer, implying a multiple of 2.1x FY22 revenue, 15.5x EV/EBITDA and ~17x P/E (vs. ~84x for the blended business).

Deal aligns with global strategy: The deal is in line with the parent's global strategy of carving out the motors business. Last year, SIEM had divested the mid-voltage (MV) business to its parent and the current deal completes the hive-off. Siemens AG, which has the IPR for the motors business, eventually plans to monetise the same either through a public offer or via a strategic investor.

Emphasis on digital growth to counter hive-off impact: SIEM is stepping up its focus on the digital business and plans to use its current base in the electrical and automation segments, where it serves close to 20 verticals including cement, steel, and food & beverage, to leverage digital growth. Management believes its exit from the LV business, where it had expected a decline, will be offset by the digital thrust.

Focus on emerging areas: SIEM is also training its focus on new and emerging areas such as fuel cells, semiconductor battery technology and solar products, where it can leverage the parent's expertise. Mobility is doing well with more railway orders expected while the acquisition of Mass-Tech Controls' electric vehicle division should help the company make inroads in the charging infrastructure space.

Outlook cautious; downgrade to HOLD: SIEM stressed that its remaining divisions should be able to offset the loss of business on account of the divestment and hence we keep our estimates unchanged. However, the deal valuation does not appear to be in favour of minority shareholders (whose approval is pending), given SIEM's current blended valuation. We, therefore, turn cautious on the stock and roll back our target FY25E P/E multiple by 20% to 52x – in line with 5Y average. This yields a reduced TP of Rs 3,700 (vs. Rs 4,500), carrying virtually no upside – downgrade from BUY to HOLD.

Key changes

Target	Rating
▼	▼

Ticker/Price	SIEM IN/Rs 3,723
Market cap	US$ 16.1bn
Free float	25%
3M ADV	US$ 14.8mn
52wk high/low	Rs 3,938/Rs 2,251
Promoter/FPI/DII	75%/5%/10%

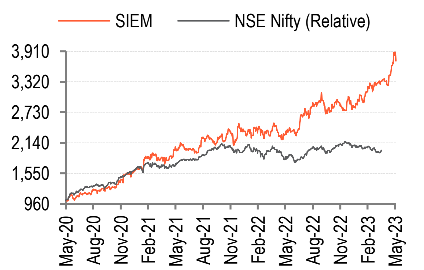
Source: NSE | Price as of 19 May 2023

Key financials

Y/E 30 Sep	FY22A	FY23E	FY24E
Total revenue (Rs mn)	1,61,378	1,96,656	2,33,094
EBITDA (Rs mn)	17,573	23,402	29,432
Adj. net profit (Rs mn)	12,619	17,228	22,202
Adj. EPS (Rs)	35.4	48.4	62.4
Consensus EPS (Rs)	35.4	47.3	61.9
Adj. ROAE (%)	11.5	14.1	16.3
Adj. P/E (x)	105.0	76.9	59.7
EV/EBITDA (x)	78.4	59.4	47.4
Adj. EPS growth (%)	22.5	36.5	28.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

CURRENCY OUTLOOK

19 May 2023

INR under pressure

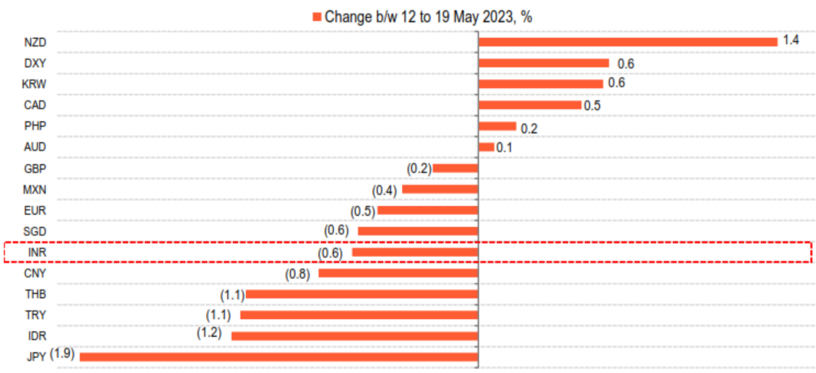
Aditi Gupta
Economist

After remaining stable for most part of the last few months, INR has come under pressure in the last few sessions. In May'23, INR has depreciated by 0.9%. However, bulk of the weakness in INR can be traced back to the last couple of sessions. In fact, since 12 May 2023 (when INR was last below the 82/$ mark), INR has depreciated by 0.6%. Prior to this, INR was fairly steady in a narrow range of 81.5-82/$. This was underpinned by robust macro fundamentals, improvement in external position, lower oil prices and buoyancy in FPI inflows.

So what are the reason behind INR's rather abrupt and sharp fall?

The most compelling reason for the rupee depreciation is a strength in dollar. In the last few sessions, dollar has once again strengthened amidst strong macro data from the US and hawkish Fed-speak. This has resulted in markets repricing the trajectory of Fed rate path. While markets widely anticipated that the Fed was done with its rate hike cycle after a final 25bps rate hike last week, macro data since then has dimmed those expectations. Strong labour market, rebound in housing sector, more than expected uptick in households' inflation expectations as well as positive developments surrounding US debt ceiling have all contributed to the belief that the Fed rate may still be behind its peak. Reinforcing this view, several Fed members have gone on record to say that inflation still remains a big challenge, warranting even higher rates. As a result, DXY has strengthened by 1.1% in the last 3 trading sessions alone. Most global currencies have seen depreciation.

Figure 1: Pressure on global currencies



Source: Bloomberg, Bank of Baroda Research | Note: Data as of 19 May 2023 16:30PM IST | Figures in bracket denote depreciation against the dollar

Another reason, though not as significant, is a moderation in FPI inflows. FPI inflows which were showing some traction since the beginning of the month have lost momentum amidst a weakness in domestic equity markets and safe haven flows.

RESULT REVIEW

BUY
TP: Rs 486 | ⮝ 16%

ITC | Consumer Staples | 19 May 2023

Strong performance amid macro headwinds

- **Growth momentum continues with 330bps YoY EBITDA margin expansion; we expect 12% topline growth in FY24**
- **FMCG business sustains healthy double-digit growth momentum at 19% YoY with steady margin improvement**
- **Continued investment in capacity and strong execution to drive growth; maintain BUY with a higher TP of Rs 486 (earlier Rs 459)**

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Strong performance across the portfolio: ITC posted 6.5% YoY revenue growth to Rs 176bn in Q4FY23 led by strong growth in cigarettes, FMCG – others, and hotels, while the paper and paperboards business slowed. The agri business remained affected by the ban on wheat and rice exports. Consolidated EBITDA margin expanded 330bps YoY (-30bps QoQ) to 35.2% despite elevated commodity prices. Adj. PAT grew 22% YoY to Rs 51bn with 360bps margin expansion. FY23 revenue/EBITDA/adj. PAT grew 17%/24%/25%. The company announced interim dividend of Rs 2.75/sh, taking the total to Rs 15.5/sh in FY23 vs. Rs 11.5/sh in FY22.

Momentum continues in cigarettes with stable margins: Cigarette revenue grew 13.7% YoY (volumes up ~12% YoY) in Q4 and continued to form ~41% of total sales, with EBIT margin stable at ~60%. Per management, stability in cigarette taxation backed by deterrent action from enforcement agencies continues to enable recovery of volumes from illicit trade, resulting in improved demand. Recent launches are steadily gaining traction along with robust growth across regions and markets.

Stellar performance in FMCG – others segment: The FMCG business is seeing sustained traction across the portfolio, with segment revenue and EBITDA growing 19% and 76% YoY respectively backed by premiumisation, judicious pricing action, supply chain agility and digital investments. Staples, biscuits, noodles, snacks, dairy, beverages, soaps and fragrances all continue to perform well.

Maintain BUY: We expect ITC to sustain its strong growth momentum across categories and accordingly model for a revenue/EBITDA/PAT CAGR of 14%/16%/16% over FY22-FY25. The cigarettes business continues to deliver double-digit volume growth and market share gains in the absence of competition from illicit trade, even as the recent tax hike is unlikely to dent sales. The FMCG – others segment too has registered healthy growth across markets and portfolios, and we expect margins to improve as input costs soften. We raise our FY24/FY25 EPS estimates by ~5% each and maintain BUY with a revised SOTP-based TP of Rs 486 (vs. Rs 459).

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	ITC IN/Rs 420
Market cap	US$ 63.5bn
Free float	71%
3M ADV	US$ 54.1mn
52wk high/low	Rs 433/Rs 259
Promoter/FPI/DII	0%/43%/57%

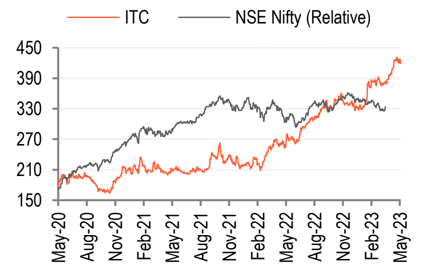
Source: NSE | Price as of 19 May 2023

Key financials

Y/E 31 Mar	FY23P	FY24E	FY25E
Total revenue (Rs mn)	7,09,369	7,94,958	8,97,358
EBITDA (Rs mn)	2,56,649	2,84,518	3,24,844
Adj. net profit (Rs mn)	1,94,039	2,12,995	2,42,377
Adj. EPS (Rs)	15.4	16.9	19.3
Consensus EPS (Rs)	15.4	15.8	17.8
Adj. ROAE (%)	27.9	29.2	31.5
Adj. P/E (x)	27.2	24.8	21.8
EV/EBITDA (x)	20.3	18.3	16.1
Adj. EPS growth (%)	22.4	9.7	13.8

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE

RESULT REVIEW

BUY

TP: Rs 729 | ⮝ 27%

STATE BANK OF INDIA | Banking | 19 May 2023

Sustaining growth and profitability

- **Lower provisioning supported robust 83% YoY PAT growth in Q4, though PPOP declined sequentially on higher opex**
- **Deposit repricing had no major impact on NIM (guided to hold at 3%); recovery in other income likely offset elevated opex**
- **We assume coverage with BUY and a TP of Rs 729 (1.3x FY25E ABV)**

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Strong Q4: SBIN's Q4FY23 PAT grew 83% YoY to Rs 167bn supported by lower provisions. PPOP dipped 2% sequentially due to higher opex, and the C/I ratio remained elevated at 55% due to provisions towards wage revision and sticky retirement benefit costs. NII grew 30% YoY (+6% QoQ), leading to 48bps (+10bps QoQ) expansion in NIM to 3.2%. Advances increased 17% YoY, beating industry growth, whereas deposits rose 9.2% YoY, resulting in a CD ratio of 72%.

Sharp reduction in credit cost: Controlled slippages and higher upgrades & recoveries helped lower credit cost to 42bps (vs. 77bps in Q3FY23 and 109bps in Q4FY22). GNPA/NNPA/PCR thus improved 36bps/10bps/27bps QoQ to 2.8%/0.7%/ 76%. SBIN's restructured book at Rs 243bn formed 0.7% of loans while SMA1&2 stood at Rs 32.6bn (-31% QoQ).

Healthy growth outlook: We model for a credit and deposit CAGR of 14.3% and 10% respectively over FY22-FY25 aided by the bank's aggressive retail centric strategy and prudent pricing (targeting high-yield assets but controlled costs). Competitive deposit pricing and a slowing overseas business are likely to keep NIM at ~3% through FY25. We estimate a 14% NII and 17% PPOP CAGR over our forecast period. Network expansion and digital integration are likely to keep C/I elevated above 50%.

Asset quality improving: SBIN's control over slippages and proactive provisioning should help it maintain a healthy asset base. A steady reduction in the restructured book (to Rs 243bn, -7% QoQ) along with a decline in SMA1/2 lend confidence, and healthy PCR at 76% (92% incl. AUCA) provides a cushion against any sudden quality shocks. We model for GNPA/NNPA improving to 2.3%/0.6% in FY25.

BUY, TP Rs 729: In view of the bank's prudent approach towards growth and margins, we expect return ratios to improve and pencil in ROA/ROE of 1%/16% in FY25. Further, with no immediate dilution plan given healthy CAR of 14.8%, we believe overall profitability has further potential to move up. Given healthy growth prospects, we assume coverage with BUY for a TP of Rs 729, based on 1.3x FY25E ABV (Gordon Growth Model) and adding in Rs 166/sh for subsidiaries.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	SBIN IN/Rs 575
Market cap	US$ 62.5bn
Free float	42%
3M ADV	US$ 124.9mn
52wk high/low	Rs 630/Rs 431
Promoter/FPI/DII	58%/10%/32%

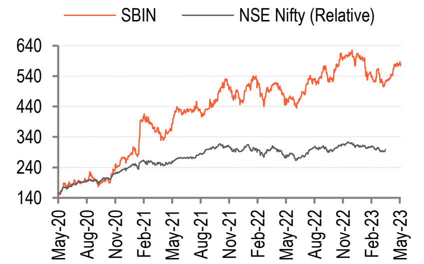
Source: NSE | Price as of 19 May 2023

Key financials

Y/E 31 Mar	FY23P	FY24E	FY25E
Net interest income	144,841	159,024	177,210
NII growth (%)	20.0	9.8	11.4
Adj. net profit (Rs mn)	50,232	55,856	62,954
EPS (Rs)	56.3	62.6	70.5
Consensus EPS (Rs)	56.3	63.5	75.3
P/E (x)	10.2	9.2	8.2
P/BV (x)	1.6	1.4	1.2
ROA (%)	1.1	1.0	1.0
ROE (%)	19.3	16.0	15.8

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE

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TRUST | INNOVATION | EXCELLENCE

BUY
TP: Rs 440 | ⮝ 34%

SYRMA SGS | Consumer Durables | 19 May 2023

Strong show; positive outlook intact

- **Q4 topline/PAT up 83%/160% YoY spurred by strong growth in the auto and consumer segments**
- **FY24 revenue growth guidance of 35-40% intact, backed by Rs 30bn order book; 8-10 key clients added in H2FY23**
- **Maintain BUY with a revised TP of Rs 440 (vs. Rs 400) on rollover**

Nilesh Patil | Vinod Chari
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Good quarter: Syrma's Q4FY23 topline at Rs 6.8bn (+83% YoY) was ~30% ahead of our estimate on strong demand traction. The EMS-led auto (+60% YoY) and consumer segments (+155%) helped offset slower growth in the healthcare (+1%) and IT divisions (+17%). EBITDA more than doubled YoY to Rs 592mn with an 8.7% margin (+190bps YoY), and PAT expanded 160% YoY to Rs 423mn. With 8-10 major client additions in H2FY23, Syrma indicated that it is on track to beat industry growth.

Strong guidance backed by expanding order book: The company's order book has expanded to Rs 30bn with fresh intake of Rs 16bn and is well diversified, per management. Additionally, contribution from railways and IT segments is likely to move up on conducive government policies. Management reiterated its revenue growth guidance of 35-40% for FY24 with potential upsides from the new IT policy. It believes a 6x asset turnover is possible once new capacities ramp up. Net working capital days are targeted to reduce to 70 on average from 74 days currently.

Operating leverage to kick in: EBITDA margin rose 190bps YoY to 8.7% in Q4 but was flattish in FY23 at 9.2% due to a higher mix of consumer business and a sharp drop in material margin to 17%. Management expects operating leverage to kick in from higher volume growth along with cost benefits from backward integration efforts.

ODM focus: Syrma raised its focus on the EMS-led auto and consumer businesses owing to better demand, since ODM's share in revenue decreased. The company has carved out an exclusive subsidiary for design & engineering-led product development, which should raise ODM contribution in the medium term, ultimately aiding the margin profile.

Maintain BUY: The strong FY23 print and upbeat guidance backed by a robust order book and expanded capacity affirm our positive stance on Syrma. Client additions offer long-term revenue visibility while strong domestic demand supports the short-term outlook, though margin expansion could be capped near term amid a thrust on EMS-led divisions. We tweak estimates and roll valuations over to Mar'25E for a higher TP of Rs 440 (vs. Rs 400), based on an unchanged 35x P/E multiple – retain BUY.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	SYRMA IN/Rs 329
Market cap	US$ 706.7mn
Free float	53%
3M ADV	US$ 1.9mn
52wk high/low	Rs 343/Rs 248
Promoter/FPI/DII	47%/5%/9%

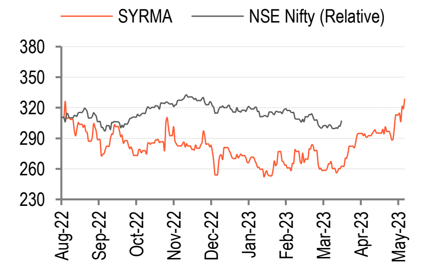
Source: NSE | Price as of 19 May 2023

Key financials

Y/E 31 Mar	FY23P	FY24E	FY25E
Total revenue (Rs mn)	20,484	26,630	36,236
EBITDA (Rs mn)	1,878	2,502	3,505
Adj. net profit (Rs mn)	1,193	1,628	2,207
Adj. EPS (Rs)	6.7	9.2	12.5
Consensus EPS (Rs)	6.7	-	-
Adj. ROAE (%)	11.3	10.1	12.4
Adj. P/E (x)	48.7	35.7	26.3
EV/EBITDA (x)	30.9	23.2	16.6
Adj. EPS growth (%)	56.1	36.5	35.5

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE

SELL
TP: Rs 585 | ⋎ 31%

THE RAMCO CEMENTS | Cement | 20 May 2023

Strong volume push but pricing pressure persists

- **New capacities (+2mt YoY) aided 45% jump in Q4 volumes (28% net of added capacities)**
- **Margin gains QoQ driven by softening of fuel cost from Rs 2.4/kcal to Rs 2.2; YoY cost remains elevated**
- **FY24/FY25 EPS raised 21%/8% on volume gains, yielding a revised TP of Rs 585 (vs. Rs 534); retain SELL on expensive valuations**

Milind Raginwar | Yash Thakur
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Volume-led topline growth: TRCL's Q4FY23 revenue grew 51%/29% YoY/QoQ to Rs 25.6bn driven by a 45%/30% YoY/QoQ jump in volumes to 4.6mt. The eastern region contributed 24% of volumes. Realisations grew just 4% YoY to Rs 5,526/t, while dipping 1% QoQ on account of pricing pressure in southern markets.

Softer energy cost QoQ: Operating cost increased 5% YoY (-4% QoQ) to Rs 4,658/t on 13% YoY energy inflation as blended fuel cost rose to Rs 2.21/kcal against Rs 1.88/kcal in Q4FY22 and Rs 2.43/kcal in Q3FY23. Additionally, raw material cost (adj. for inventory) grew 36%/47% YoY/QoQ to Rs 1,147/t. Other expenditure increased just 5%/4% YoY/QoQ to Rs 2.4bn despite the strong volume push as the company benefited from improved operating leverage. Logistics cost declined 2%/3% YoY/QoQ to Rs 1,079/t as the average lead distance came down.

Strong EBITDA gains: EBITDA rose 40%/45% YoY/QoQ to Rs 4.1bn and margin improved 190bps QoQ but declined 120bps YoY to 16.1% due to higher energy cost. EBITDA/t dipped 4% YoY to Rs 870/t and grew 13% QoQ. Reported PAT of Rs 1.5bn grew 23%/126% YoY/QoQ despite higher interest expense and depreciation.

Capacity expansion plans: Commissioning timelines are as follows – Odisha grinding unit line II with 0.9mtpa of cement capacity: H2FY24, 4MW of Waste Heat Recovery System capacity in Kurnool: 18MW thermal power plant and railway siding: FY24, and two dry mortar plant units in Andhra Pradesh and Odisha: FY24. Management indicated that the next phase of expansion will begin with Kurnool line II (3mt cement, 2.25mt clinker), followed by the Karnataka greenfield plant.

Valuations high; retain SELL: TRCL's volume-driven growth is likely to continue, albeit tempered by pricing pressure. Based on the Q4 print, we raise our FY24/FY25 EPS estimates by 21%/8%. Even so, current valuations of 13.9x FY25E EV/EBITDA look expensive given TRCL's high gearing, single-digit return ratios and weak margin profile. We thus retain SELL, valuing the stock at an unchanged 10x FY25E EV/EBITDA multiple, which implies a replacement cost of Rs 8.1bn/mt – a 10% premium to the industry average. Post estimate revision, our TP moves to Rs 585 (vs. Rs 534).

Key changes

Target	Rating
▲	◄ ►

Ticker/Price	TRCL IN/Rs 844
Market cap	US$ 2.4bn
Free float	58%
3M ADV	US$ 4.3mn
52wk high/low	Rs 850/Rs 576
Promoter/FPI/DII	42%/7%/32%

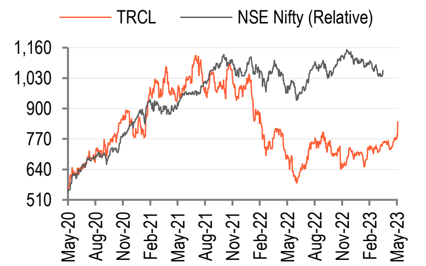
Source: NSE | Price as of 19 May 2023

Key financials

Y/E 31 Mar	FY23P	FY24E	FY25E
Total revenue (Rs mn)	81,353	93,036	1,04,850
EBITDA (Rs mn)	11,479	14,657	17,443
Adj. net profit (Rs mn)	3,095	4,992	6,590
Adj. EPS (Rs)	13.1	21.1	27.9
Consensus EPS (Rs)	13.1	26.0	32.5
Adj. ROAE (%)	4.6	7.1	8.8
Adj. P/E (x)	64.4	39.9	30.3
EV/EBITDA (x)	21.1	16.4	13.9
Adj. EPS growth (%)	(65.4)	61.3	32.0

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE

RESULT REVIEW

SELL

TP: Rs 3,000 | ⩔ 9%

ALKEM LABS | Pharmaceuticals | 20 May 2023

Margin improvement key for revival

- **Q4 EBITDA/PAT of Rs 3.5bn/Rs 710mn well short of consensus by 21%/ 79% primarily due to higher operating costs**
- **Increased sales and marketing spend, field force addition and US price erosion ate into margins**
- **Insipid US sales remain a challenge; maintain SELL with an unchanged TP of Rs 3,000**

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Strong India growth on launches: Alkem's Q4FY23 EBITDA/PAT missed consensus estimates by 21%/79% due to higher operating costs, despite revenue being a 6% beat. Revenue/EBITDA/PBT grew 17%/5%/22% YoY to Rs 29bn/Rs 3.5bn/Rs 3.1bn but fell sequentially (-5%/-41%/-42%). India business outperformed the market despite a high base, led by strong growth in anti-infectives (+30% YoY), pain (23%), respiratory (27%), and dermatology (34%) therapies in the acute space, while chronic therapies such as anti-diabetic (+37%) and neuro (+36%) also fared well with market-beating growth. The recent launch of Sitagliptin helped the anti-diabetic portfolio in Q4.

Steep QoQ decline in US business: US revenue plunged 22% QoQ to US$ 72mn due to a high base on account of one-time seasonal benefits in the previous quarter. Revenue grew 9% YoY (-22% QoQ) in rupee terms. Alkem's US business remains under significant pricing pressure with double-digit erosion. Management expects price erosion to stabilise at high single digits. The company has discontinued the St. Louis facility in the US (<2% contribution) as part of cost optimisation.

Cost controls guided to aid margin expansion: Gross/EBITDA margins contracted 170bps/140bps YoY to 56.7%/12.2% (-220bps/-750bps QoQ), with a steeper sequential decline on account of tailwinds from the US flu season in Q3. Overheads costs increased 32% YoY (+20% QoQ) to 22.2% of revenue in Q4 from 17.7%/19.6% in Q3FY23/Q4FY22. Alkem also incurred a one-time loss of Rs 1bn on account of fixed asset impairment at the St. Louis facility. Management has guided for 200bps EBITDA margin improvement to 16% in FY24 on the back of cost optimisation measures.

Maintain SELL: Relentless price erosion in the US market, elevated input costs and higher marketing spends have taken a toll on Alkem's margins through FY23. This apart, we expect the US business to remain sluggish as investments are recalibrated amid challenges to growth. We maintain our TP at Rs 3,000 based on an unchanged 15x FY25E EV/EBITDA multiple – a 15% discount to the stock's 5Y average – and retain SELL given 9% downside potential from the current price.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	ALKEM IN/Rs 3,302
Market cap	US$ 4.8bn
Free float	41%
3M ADV	US$ 6.3mn
52wk high/low	Rs 3,625/Rs 2,855
Promoter/FPI/DII	57%/4%/17%

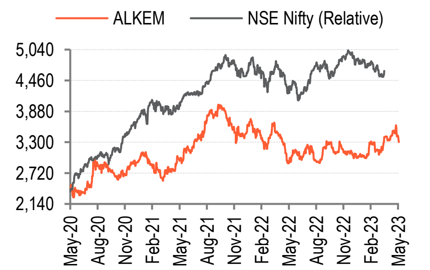
Source: NSE | Price as of 19 May 2023

Key financials

Y/E 31 Mar	FY23P	FY24E	FY25E
Total revenue (Rs mn)	1,15,993	1,31,675	1,45,175
EBITDA (Rs mn)	16,095	20,510	23,506
Adj. net profit (Rs mn)	10,872	15,902	18,632
Adj. EPS (Rs)	90.9	133.0	155.9
Consensus EPS (Rs)	90.9	133.4	161.4
Adj. ROAE (%)	14.4	19.1	19.6
Adj. P/E (x)	36.3	24.8	21.2
EV/EBITDA (x)	24.4	18.9	16.0
Adj. EPS growth (%)	(34.5)	46.3	17.2

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE

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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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