

BUY

TP: Rs 630 | ▲ 23%

LAURUS LABS

Pharmaceuticals

30 April 2020

Good beat; firm FY21 outlook – target raised to Rs 630

Laurus Labs reported a strong operational beat of 8%/20%/41% on sales/EBITDA/PBT in Q4. Key drivers were the synthesis and other API businesses, alongside stable gross margins of 50%. EBITDA stood at Rs 1.9bn with 22.8% margins. Benefit of HCQS supplies will reflect from Q1. Overall, Laurus expects to sustain the momentum in FY21, backed by strong order visibility in formulations. Focus on margins, return ratios and positive FCF continues. We raise FY21/FY22 EBITDA 4-5% and revise our Mar'21 TP from Rs 510 to Rs 630 (10x FY22E EV/EBITDA).

Vivek Kumar
research@bobcaps.in

FY20 impressive but FY21/FY22 can see equally strong growth: The shift towards a high-margin product mix led to an operationally strong FY20, with 58% EBITDA growth, 20% margins (+400bps over FY19) and 13% ROCE (+5ppt). This momentum is expected to sustain and predictability in the business has also risen substantially with the ex-ARV sales mix at 64% (vs. 39% in FY19). Further, a strong order book in FDF and non-ARV APIs (oncology, cardio-diabetic), TLE400/600mg FDA approvals in H1FY21, and offtake in non-Aspen CDMO contracts are key levers, driving ~20% EBITDA growth for FY20E-FY23E.

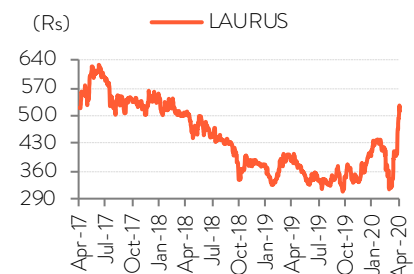
Formulations (FDF) execution remains key: In our view, FDF clocked >20% EBITDA margins in FY20 – we see expansion potential of at least 3-4ppt over the next 2-3 years as sales shift from EM-LMIC tenders to US and EU generics. With solid orders in hand, Laurus is doubling FDF capacity by FY22 via brownfield expansion (incurring Rs 3.3bn in capex for FY21 – ATR could be 1.5-2x). We expect US\$ 140mn/160mn of FDF sales in FY21/FY22.

Earnings call highlights: (1) Expect growth recovery in ARV business in FY21 as pricing has stabilised. (2) Strong Q4 margin led by product mix and volumes. (3) Working on Favipiravir APIs and formulations with a partner. (4) Oncology API sales growth to normalise from H1FY21. (5) announced stock split of 1:5.

Ticker/Price	LAURUS IN/Rs 513
Market cap	US\$ 726.3mn
Shares o/s	106mn
3M ADV	US\$ 2.0mn
52wk high/low	Rs 536/Rs 295
Promoter/FPI/DII	32%/37%/5%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
Total revenue (Rs mn)	20,562	22,919	28,301	33,002	37,403
EBITDA (Rs mn)	4,134	3,560	5,607	6,768	7,973
Adj. net profit (Rs mn)	1,483	937	2,582	2,968	3,587
Adj. EPS (Rs)	13.9	8.8	24.3	27.9	33.7
Adj. EPS growth (%)	(10.8)	(36.8)	175.5	14.9	20.9
Adj. ROAE (%)	10.5	6.2	15.4	15.3	16.0
Adj. P/E (x)	36.8	58.2	21.1	18.4	15.2
EV/EBITDA (x)	15.5	18.1	11.6	9.8	8.4

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	Q3FY20E	Var. (%)	FY20P	FY19	YoY (%)
Net Sales	8,390	6,351	32.1	7,295	15.0	7,750	8.3	28,315	22,917	23.6
EBITDA	1,917	1,119	71.3	1,483	29.3	1,600	19.8	5,612	3,560	57.6
Depreciation	460	434	-	476	-	470	-	1,872	1,641	-
EBIT	1,457	685	-	1,007	-	1,130	-	3,740	1,919	-
Interest	207	176	-	208	-	238	-	896	881	-
Other Income	17	16	-	19	-	10	-	95	161	-
PBT	1,267	525	141.4	818	54.9	902	40.5	2,939	1,199	145.1
Less: Taxation	166	94	-	82	-	235	-	383	260	-
Less: Minority Interest	0	0	-	0	-	0	-	0	0	-
Recurring PAT	1,102	431	155.5	736	49.7	668	65.0	2,556	939	172.2
Exceptional items	0	0	-	0	-	0	-	-	-	-
Reported PAT	1,102	431	155.5	736	49.7	668	65.0	2,556	939	172.2
Key Ratios (%)										
Gross Margin	50.1	46.2	-	50.6	-	50.8	-	50.6	50.6	-
EBITDA Margin	22.8	17.6	-	20.3	-	20.6	-	19.8	15.5	-
Tax / PBT	13.1	17.9	-	10.1	-	26.0	-	13.0	21.7	-
NPM	13.1	6.8	-	10.1	-	8.6	-	9.0	4.1	-
EPS (Rs)	10.4	4.1	-	6.9	-	6.3	-	23.9	8.8	-

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	Q3FY20E	Var. (%)	FY20P	FY19	YoY (%)
Generics – API	4,239	4,927	(14.0)	3,578	18.5	3,598	17.8	16,138	19,190	(15.9)
ARVs	2,645	3,153	(16.1)	1,980	33.6	2,000	32.3	10,329	13,956	(26.0)
Hep C	83	415	(80.0)	155	(46.5)	155	(46.5)	533	1,172	(54.5)
Oncology	591	708	(16.5)	468	26.3	743	(20.5)	2,106	2,173	(3.1)
Other API	920	651	41.3	975	(5.6)	700	31.4	3,170	1,889	67.8
Synthesis	1,259	940	33.9	617	104.1	1,128	11.6	3,069	2,550	20.4
Ingredients	220	203	8.4	179	22.9	223	(1.5)	856	632	35.5
Formulations	2,673	282	847.9	2,921	(8.5)	2,800	(4.5)	8,253	549	1,403.6
Net Sales	8,391	6,352	32.1	7,295	15.0	7,750	8.3	28,315	22,920	23.5

Source: Company, BOBCAPS Research

Valuation methodology

We retain our investment thesis on Laurus following a consistent increase in EBITDA share from high-margin businesses (synthesis, formulations, other APIs ex-ARV) and sharp turnaround in return ratios which could re-rate the stock in coming years. In the next two years, these high-margin segments are expected to drive >80% of incremental EBITDA and ROCE of >16% from ~13% in FY20. While incremental capex timelines have been advanced by a year (led by solid execution on formulations which is ahead of schedule), this would not be FCF-dilutive in our view.

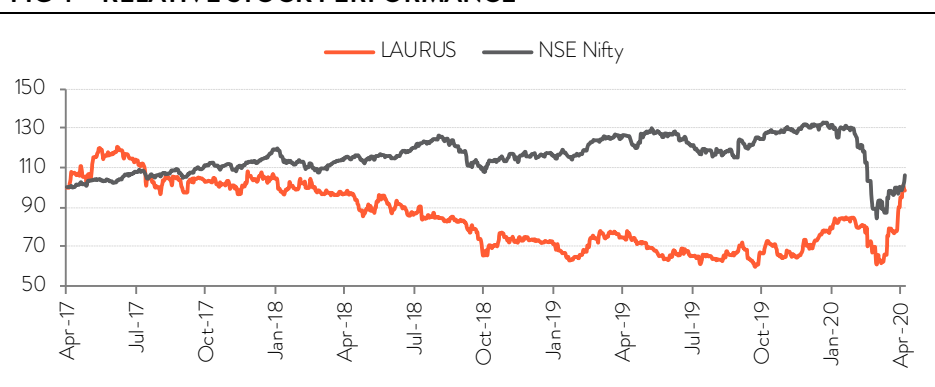
Laurus has rallied 50% from the recent Mar'20 bottom and is trading at 8.3x FY22E EBITDA, which is still below the three-year historical mean of 12x one-year forward. We raise our target EV/EBITDA multiple to 10x (from 9x) on FY22E, which is a 35-40% discount to large-cap peers. We also increase our FY21/FY22 EBITDA forecasts by 4%/5% to factor in the full-year beat and positive outlook, translating to a revised Mar'21 target price of Rs 630 (from Rs 510). Maintain BUY.

FIG 3 – REVISED ESTIMATES

(Rs bn)	New			Old			Change (%)		
	FY20P	FY21E	FY22E	FY20P	FY21E	FY22E	FY20P	FY21E	FY22E
Sales	28.3	33.0	37.4	27.5	31.9	35.7	2.9	3.5	4.7
EBITDA	5.6	6.8	8.0	5.1	6.5	7.6	10.4	3.6	4.7
EBITDA margin (%)	19.8	20.5	21.3	18.5	20.5	21.3	134bps	2bps	(0bps)
EPS (Rs)	24	28	34	16	25	31	56.5	11.4	9.8

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Higher concentration and pricing pressure in ARVs:** The ARV segment accounted for 36% of revenues in FY20 (from 61% in FY19) and has witnessed pricing pressure in the past two years. A shift in the treatment regime from Efavirenz to Dolutegravir has adversely impacted gross margins. To arrest the margin compression and business decline in ARV, management has taken steps toward: (1) backward integration of some APIs including FTC and Lamivudine, and (2) rapid expansion of the non-ARV business. This, in our view, should mitigate the profitability risk.
- **Regulatory risks:** Units 1 and 3 are critical as they account for 80% of the topline (mainly catering to the API and synthesis businesses). Unit 2 is Laurus' sole US formulations facility. All three units have recently received establishment inspection reports (EIR).
- **Delay in formulation business ramp-up:** Any delays in product approval can adversely affect the planned scale-up and our FY21 forecast.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Total revenue	20,562	22,919	28,301	33,002	37,403
EBITDA	4,134	3,560	5,607	6,768	7,973
Depreciation	1,254	1,642	1,872	2,109	2,362
EBIT	2,880	1,918	3,735	4,660	5,612
Net interest income/(expenses)	(796)	(882)	(896)	(1,078)	(1,026)
Other income/(expenses)	98	161	95	38	72
Exceptional items	0	0	0	0	0
EBT	2,182	1,197	2,935	3,620	4,658
Income taxes	698	260	352	652	1,071
Extraordinary items	194	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	1,678	937	2,582	2,968	3,587
Adjustments	194	0	0	0	0
Adjusted net profit	1,483	937	2,582	2,968	3,587

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Accounts payables	3,123	4,882	4,652	4,973	5,636
Other current liabilities	1,488	1,411	1,981	2,310	2,618
Provisions	253	365	451	526	596
Debt funds	10,477	11,068	12,686	12,670	11,465
Other liabilities	0	0	0	0	0
Equity capital	1,060	1,064	1,064	1,064	1,064
Reserves & surplus	13,764	14,517	16,915	19,684	23,071
Shareholders' fund	14,824	15,581	17,980	20,748	24,136
Total liabilities and equities	30,165	33,307	37,750	41,227	44,451
Cash and cash eq.	31	30	17	668	712
Accounts receivables	5,705	7,099	7,914	8,590	9,735
Inventories	5,847	6,819	9,052	9,494	10,760
Other current assets	2,108	1,939	3,113	3,630	4,114
Investments	34	34	34	34	34
Net fixed assets	14,639	16,072	16,305	17,497	17,781
CWIP	1,632	1,096	1,096	1,096	1,096
Intangible assets	169	218	218	218	218
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	30,165	33,307	37,750	41,227	44,451

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Net income + Depreciation	2,932	2,579	4,454	5,077	5,948
Interest expenses	0	0	2	0	0
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(205)	(402)	(3,796)	(910)	(1,854)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	2,727	2,177	660	4,167	4,094
Capital expenditures	(3,753)	(3,117)	(2,105)	(3,300)	(2,646)
Change in investments	0	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(3,753)	(3,117)	(2,105)	(3,300)	(2,646)
Equities issued/Others	2	4	0	0	0
Debt raised/repaid	1,385	591	1,618	(16)	(1,205)
Interest expenses	0	0	(2)	0	0
Dividends paid	(190)	(176)	(184)	(200)	(200)
Other financing cash flows	(182)	519	0	0	0
Cash flow from financing	1,015	939	1,433	(216)	(1,405)
Changes in cash and cash eq.	(10)	(1)	(13)	652	44
Closing cash and cash eq.	31	29	17	668	712

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20P	FY21E	FY22E
Reported EPS	15.8	8.8	24.3	27.9	33.7
Adjusted EPS	13.9	8.8	24.3	27.9	33.7
Dividend per share	1.5	1.5	1.5	1.5	1.5
Book value per share	139.3	146.4	168.9	194.9	226.8

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20P	FY21E	FY22E
EV/Sales	3.1	2.8	2.3	2.0	1.8
EV/EBITDA	15.5	18.1	11.6	9.8	8.4
Adjusted P/E	36.8	58.2	21.1	18.4	15.2
P/BV	3.7	3.5	3.0	2.6	2.3

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20P	FY21E	FY22E
Tax burden (Net profit/PBT)	68.0	78.3	88.0	82.0	77.0
Interest burden (PBT/EBIT)	75.8	62.4	78.6	77.7	83.0
EBIT margin (EBIT/Revenue)	14.0	8.4	13.2	14.1	15.0
Asset turnover (Revenue/Avg TA)	21.6	22.1	24.7	25.7	27.1
Leverage (Avg TA/Avg Equity)	1.7	1.7	1.7	1.7	1.5
Adjusted ROAE	10.5	6.2	15.4	15.3	16.0

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

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
YoY growth (%)					
Revenue	8.0	11.5	23.5	16.6	13.3
EBITDA	1.4	(13.9)	57.5	20.7	17.8
Adjusted EPS	(10.8)	(36.8)	175.5	14.9	20.9
Profitability & Return ratios (%)					
EBITDA margin	20.1	15.5	19.8	20.5	21.3
EBIT margin	14.0	8.4	13.2	14.1	15.0
Adjusted profit margin	7.2	4.1	9.1	9.0	9.6
Adjusted ROAE	10.5	6.2	15.4	15.3	16.0
ROCE	12.5	8.0	13.4	14.7	16.5
Working capital days (days)					
Receivables	101	113	102	95	95
Inventory	103	109	117	105	105
Payables	55	78	60	55	55
Ratios (x)					
Gross asset turnover	1.1	1.1	1.2	1.2	1.3
Current ratio	2.8	2.4	2.8	2.9	2.9
Net interest coverage ratio	3.6	2.2	4.2	4.3	5.5
Adjusted debt/equity	0.7	0.7	0.7	0.6	0.4

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

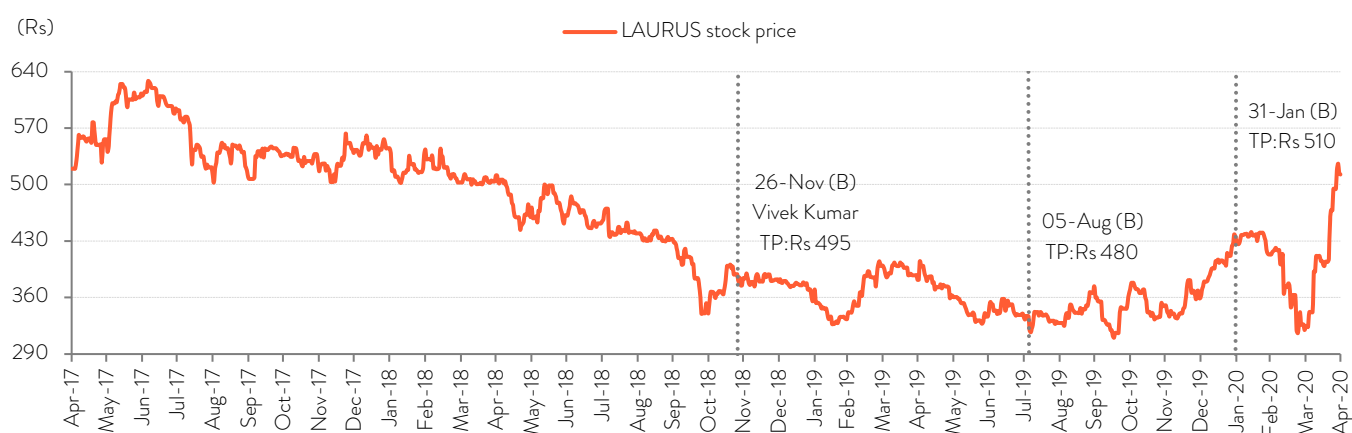
ADD – Expected return from >+5% to +15%

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: LAURUS LABS (LAURUS IN)



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

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