

BUY

TP: Rs 540 | ▲ 19%

LAURUS LABS

Pharmaceuticals

01 May 2021

Solid margins despite higher API mix

Laurus Labs reported yet another strong quarter on the back of high growth in the API (esp. ARV) and formulation segments. Q4FY21 revenue and EBITDA beat consensus by 4% each. EBITDA grew 146% YoY (11% QoQ) with margins at 33.4%, aided by a better mix and operating leverage. Formulation (FDF) sales grew 61% YoY and ARVs 109% YoY (flat QoQ). Laurus expects to sustain a 30% EBITDA margin and has raised FY22/FY23 capex to Rs 15bn-17bn. We increase FY22-FY23 EPS 7-9% and revise our Mar'22 TP to Rs 540 (vs. Rs 480).

Saad Shaikh

research@bobcaps.in

Healthy demand and solid execution: Laurus' ARV segment contributed half of incremental sales in Q4FY21, growing at 109% YoY to Rs 5.7bn as demand for third-party APIs increased. The company is still expanding API capacity to serve existing demand from customers and expects good sales in FY22 as well.

Robust margins: Q4/FY21 gross margins were strong at ~55% each. EBITDA margins came in at 33.4%/32.2% due to a better product mix and operating leverage. Management expects to maintain a 30% EBITDA margin in FY22.

FDF debottlenecking completed: FDF grew 61% YoY (~30% share of incremental sales), with higher LMIC market volumes as well as increased volumes from North America and the EU. Added capacity from debottlenecking will be available from Q1FY22. Custom synthesis grew 19% YoY (39% QoQ) on the back of commercial and late-stage clinical supplies. Other APIs grew 80% YoY (68% QoQ) due to higher volumes and capacity addition.

Maintain BUY: We retain BUY on Laurus following a consistent increase in EBITDA share from high-margin businesses and turnaround in return ratios. We raise FY22-FY23 EBITDA by 11-12% to factor in the solid FY21 beat and higher gross margins. Our Mar'22 TP rises to Rs 540 at an unchanged 14x EV/EBITDA.

Ticker/Price	LAURUS IN/Rs 453
Market cap	US\$ 3.3bn
Shares o/s	537mn
3M ADV	US\$ 20.1mn
52wk high/low	Rs 483/Rs 84
Promoter/FPI/DII	27%/21%/4%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21P	FY22E	FY23E
Total revenue (Rs mn)	22,919	28,317	48,135	58,600	68,300
EBITDA (Rs mn)	3,560	5,645	15,507	18,229	21,304
Adj. net profit (Rs mn)	937	2,553	9,836	11,861	13,864
Adj. EPS (Rs)	1.7	4.8	18.3	22.1	25.8
Adj. EPS growth (%)	(36.8)	172.3	285.3	20.6	16.9
Adj. ROAE (%)	6.2	15.3	45.0	37.8	32.0
Adj. P/E (x)	259.2	95.2	24.7	20.5	17.5
EV/EBITDA (x)	71.0	44.9	16.4	14.1	12.1

Source: Company, BOBCAPS Research | P – Provisional

BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda

Important disclosures, including any required research certifications, are provided at the end of this report.



FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)	Cons.	Var. (%)	FY21	FY20	YoY (%)
Net Sales	14,119	8,390	68.3	12,884	9.6	13,584	3.9	48,135	28,315	70.0
EBITDA	4,722	1,917	146.3	4,263	10.8	4,560	3.6	15,509	5,612	176.4
Depreciation	536	460	-	516	-	-	-	2,051	1,872	-
EBIT	4,186	1,457	-	3,747	-	-	-	13,458	3,740	-
Interest	219	207	-	174	-	-	-	681	896	-
Other Income	45	17	-	69	-	-	-	237	95	-
PBT	4,012	1,267	216.6	3,642	10.2	3,870	3.7	13,013	2,939	342.8
Less: Taxation	1,043	166	-	913	-	-	-	3,173	383	-
Less: Minority Interest	0	0	-	0	-	-	-	0	0	-
Recurring PAT	2,969	1,102	169.6	2,729	8.8	2,962	0.2	9,841	2,556	285.1
Exceptional items	0	0	-	0	-	-	-	-	-	-
Reported PAT	2,969	1,102	169.6	2,729	8.8	2,962	0.2	9,841	2,556	285.1
Key Ratios (%)			(bps)		(bps)					(bps)
Gross Margin	55.5	50.1	540	54.7	79	-	-	55.2	50.1	508
EBITDA Margin	33.4	22.8	1,059	33.1	36	33.6	-	32.2	19.8	1,240
Tax / PBT	26.0	13.1	-	25.1	-	-	-	24.4	13.0	-
NPM	21.0	13.1	-	21.2	-	21.8	-	20.4	9.0	1,142
EPS (Rs)	5.5	2.1	-	5.1	-	5.5	-	18.3	4.8	-

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)	FY21	FY20	YoY (%)
Generics – API	7,970	4,239	88.0	7,310	9.0	26,210	15,680	67.2
ARVs	5,690	2,728	108.6	5,680	0.2	18,520	10,329	79.3
Oncology	620	591	4.9	640	-3.1	2,630	2,106	24.9
Other API	1,660	920	80.4	990	67.7	5,060	3,245	55.9
Synthesis	1,760	1,479	19.0	1,270	38.6	5,190	3,850	34.8
Formulations	4,300	2,673	60.9	4,300	0.0	16,640	8,253	101.6
Net Sales	14,030	8,391	67.2	12,880	8.9	48,040	27,783	72.9

Source: Company, BOBCAPS Research

Earnings call highlights

- **Margins:** Management is optimistic of 30% EBITDA margin for FY22. Laurus expects to grow revenue by higher volume offtake rather than price hikes. It did not take any hikes in FY21 and has none planned for FY22 either.
- **Capex:** FY21 capex was at Rs 7bn and combined capex for FY22 and FY23 has been revised up to Rs 15bn-17bn from Rs 12bn earlier, which will be funded by internal accruals. Of the total capex, 50% is earmarked for API and 25% each for the formulation and synthesis businesses.
- **R&D:** The company spent Rs 1.8bn (~4 % of sales) on R&D in FY21.
- **Revenue target:** The company has an internal revenue target of US\$ 1bn by FY23.
- **FDf:** Laurus commenced marketing of in-licensed products in the US to leverage front-end capabilities, starting with two of five products. The rest will follow in six months. It expects to file 8-10 ANDAs next year in the US generics space. Debottlenecking of the formulations facility was completed in March and the additional capacity will be utilised in Q1/Q2 of FY22.
- **CDMO:** The company has 50 active projects for its custom synthesis (CDMO) division and aims to win contracts from global pharmaceutical companies and several late-stage projects to scale up focus on this premium business. It is in discussions with key generic partners to tap into the contract manufacturing opportunity. Two additional products have been validated as part of the company's CDMO expansion in the EU. Management expects custom synthesis to outpace other divisions by FY23, after the Vizag plant is completed.
- **Laurus Bio:** The acquired Richcore (Laurus Bio) facility will be partly commercialised by May 15 (two fermenters) and by September, the entire facility (two more fermenters) will be live. Fermentation capacity is at 45,000ltr per unit for which the order book is in place. Laurus plans to develop an additional 1mn ltr of capacity. It is looking to use the newly acquired biotech capacity to diversify into recombinant products, which are made via the use of genetically engineered DNA. Management expects two-fold revenue growth from this facility in FY22.
- **Diversification:** Growth will be driven by the non-ARV business from FY23 onwards. The company is entering into the diabetic and cardiovascular segments, which will be commercialised in the last quarter of FY22. Brownfield expansion in formulations is also in the non-ARV segment.

Valuation methodology

We retain our BUY rating 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 spur a stock rerating in coming years. Over the next two years, these high-margin segments – supported by recalibration in the procurement strategies of global companies – are expected to drive >90% of incremental EBITDA and aid sustained ROIC of >35% for Laurus from ~14% in FY20.

Given the solid order book and ahead-of-schedule execution, the company has increased its total planned capex to Rs 15bn-17bn for FY22/FY23 combined (from Rs 12bn). This should be viewed positively as incremental capex would not be FCF-dilutive, in our view.

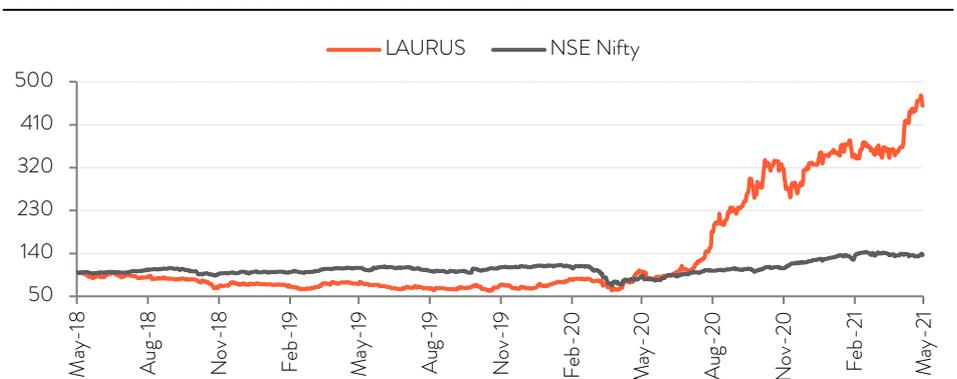
The share price has rallied sharply, more than tripling from Mar'20 lows, but current valuations of 12x FY23E EBITDA are still in-line with the three-year historical mean of 12x one-year forward. We increase our FY22-FY23 EBITDA forecasts by 11-12% to factor in the solid FY21 beat, higher gross margins and sustainable rise in operating leverage. Our Mar'22 target price rises to Rs 540 (from Rs 480) as we revise our estimates, based on an unchanged one-year forward EV/EBITDA multiple of 14x.

FIG 3 – REVISED ESTIMATES

(Rs bn)	New		Old		Change (%)	
	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Sales	58.6	68.3	51.1	58.3	14.7	17.2
EBITDA	18.2	21.3	16.5	19.1	10.7	11.7
EBITDA margin (%)	31.1	31.2	32.2	32.7	(111bps)	(152bps)
EPS (Rs)	22	26	20	24	8.9	7.2

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Higher concentration and pricing pressure in ARVs:** The ARV segment accounted for 39% of revenues in FY21 (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 ARVs, 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 hence our FY21 forecast for the formulations business.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Total revenue	22,919	28,317	48,135	58,600	68,300
EBITDA	3,560	5,645	15,507	18,229	21,304
Depreciation	1,642	1,873	2,051	2,392	2,917
EBIT	1,918	3,773	13,456	15,837	18,387
Net interest income/(expenses)	(882)	(896)	(682)	(901)	(755)
Other income/(expenses)	161	59	237	78	143
Exceptional items	0	0	0	0	0
EBT	1,197	2,936	13,011	15,014	17,774
Income taxes	260	383	3,173	3,153	3,910
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	2	0	0
Reported net profit	937	2,553	9,836	11,861	13,864
Adjustments	0	0	0	0	0
Adjusted net profit	937	2,553	9,836	11,861	13,864

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Accounts payables	4,882	6,156	11,787	12,041	14,034
Other current liabilities	1,411	1,625	3,158	4,102	4,098
Provisions	365	568	757	921	1,073
Debt funds	11,068	11,456	15,799	14,233	10,949
Other liabilities	0	0	0	0	0
Equity capital	1,064	1,069	1,073	1,073	1,073
Reserves & surplus	14,517	16,623	24,934	35,757	48,615
Shareholders' fund	15,581	17,692	26,007	36,830	49,688
Total liabilities and equities	33,307	37,497	57,507	68,128	79,842
Cash and cash eq.	30	17	485	1,013	1,769
Accounts receivables	7,099	7,914	13,061	15,252	18,525
Inventories	6,819	9,052	15,755	18,463	22,081
Other current assets	1,939	2,545	2,845	2,930	3,415
Investments	34	34	34	34	34
Net fixed assets	16,072	17,068	19,150	24,258	28,840
CWIP	1,096	672	3,622	3,622	2,622
Intangible assets	218	195	2,556	2,556	2,556
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	33,307	37,497	57,507	68,128	79,842

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21P	FY22E	FY23E
Net income + Depreciation	2,579	4,425	11,887	14,254	16,781
Interest expenses	0	0	0	0	0
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(402)	(1,963)	(4,797)	(3,622)	(5,234)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	2,177	2,462	7,089	10,632	11,547
Capital expenditures	(3,117)	(2,374)	(7,000)	(7,500)	(7,500)
Change in investments	0	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(3,117)	(2,374)	(7,000)	(7,500)	(7,500)
Equities issued/Others	4	5	4	0	0
Debt raised/repaid	591	388	4,343	(1,566)	(3,285)
Interest expenses	0	0	0	0	0
Dividends paid	(176)	0	(1,006)	(1,006)	(1,006)
Other financing cash flows	519	(493)	(2,962)	(31)	1,000
Cash flow from financing	939	(100)	379	(2,603)	(3,291)
Changes in cash and cash eq.	(1)	(13)	468	529	756
Closing cash and cash eq.	29	17	485	1,013	1,769

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21P	FY22E	FY23E
Reported EPS	1.7	4.8	18.3	22.1	25.8
Adjusted EPS	1.7	4.8	18.3	22.1	25.8
Dividend per share	1.5	1.5	1.5	1.5	1.5
Book value per share	29.0	33.0	48.4	68.6	92.6

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21P	FY22E	FY23E
EV/Sales	11.0	9.0	5.3	4.4	3.8
EV/EBITDA	71.0	44.9	16.4	14.1	12.1
Adjusted P/E	259.2	95.2	24.7	20.5	17.5
P/BV	15.6	13.7	9.4	6.6	4.9

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21P	FY22E	FY23E
Tax burden (Net profit/PBT)	78.3	86.9	75.6	79.0	78.0
Interest burden (PBT/EBIT)	62.4	77.8	96.7	94.8	96.7
EBIT margin (EBIT/Revenue)	8.4	13.3	28.0	27.0	26.9
Asset turnover (Revenue/Avg TA)	22.1	25.4	33.9	31.5	30.6
Leverage (Avg TA/Avg Equity)	1.7	1.7	1.6	1.5	1.3
Adjusted ROAE	6.2	15.3	45.0	37.8	32.0

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21P	FY22E	FY23E
YoY growth (%)					
Revenue	11.5	23.6	70.0	21.7	16.6
EBITDA	(13.9)	58.6	174.7	17.6	16.9
Adjusted EPS	(36.8)	172.3	285.3	20.6	16.9
Profitability & Return ratios (%)					
EBITDA margin	15.5	19.9	32.2	31.1	31.2
EBIT margin	8.4	13.3	28.0	27.0	26.9
Adjusted profit margin	4.1	9.0	20.4	20.2	20.3
Adjusted ROAE	6.2	15.3	45.0	37.8	32.0
ROCE	8.0	13.7	38.6	34.3	33.2
Working capital days (days)					
Receivables	113	102	99	95	99
Inventory	109	117	119	115	118
Payables	78	79	89	75	75
Ratios (x)					
Gross asset turnover	1.1	1.2	1.6	1.5	1.5
Current ratio	2.4	2.3	2.0	2.2	2.4
Net interest coverage ratio	2.2	4.2	19.7	17.6	24.3
Adjusted debt/equity	0.7	0.6	0.6	0.4	0.2

Source: Company, BOBCAPS Research

Disclaimer

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

BUY – Expected return >+15%

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

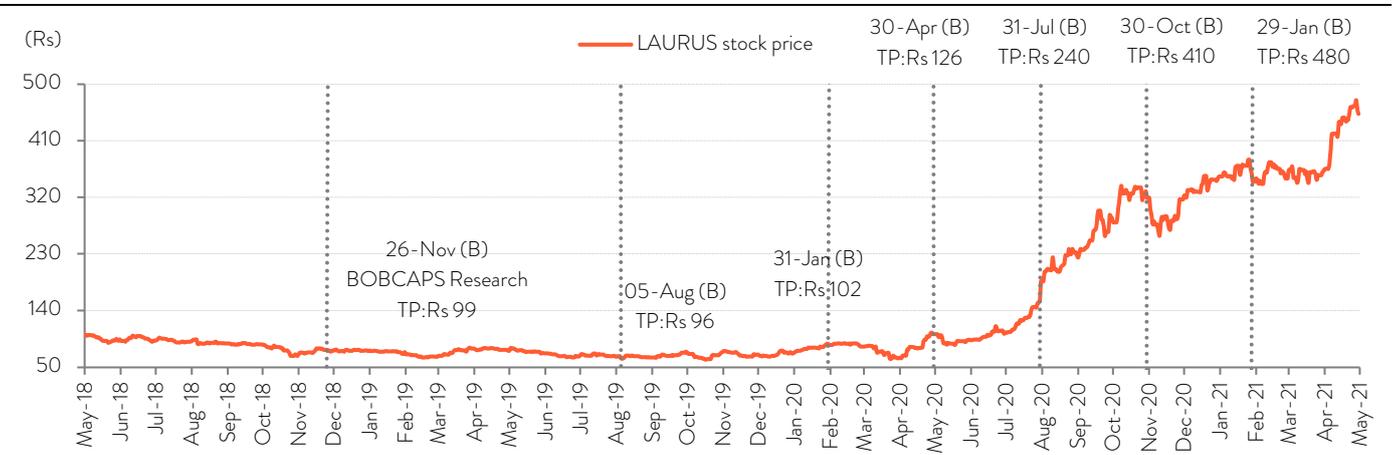
REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

RATINGS AND TARGET PRICE (3-YEAR HISTORY): LAURUS LABS (LAURUS IN)



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

Rating distribution

As of 30 April 2021, out of 90 rated stocks in the BOB Capital Markets Limited (BOBCAPS) coverage universe, 43 have BUY ratings, 16 have ADD ratings, 5 are rated REDUCE and 26 are rated SELL. None of these companies have been investment banking clients in the last 12 months.

Analyst certification

The research analyst(s) authoring this report hereby certifies that (1) all of the views expressed in this research report accurately reflect his/her personal views about the subject company or companies and its or their securities, and (2) no part of his/her compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) in this report. Analysts are not registered as research analysts by FINRA and are not associated persons of BOBCAPS.

General disclaimers

BOBCAPS is engaged in the business of Institutional Stock Broking and Investment Banking. BOBCAPS is a member of the National Stock Exchange of India Limited and BSE Limited and is also a SEBI-registered Category I Merchant Banker. BOBCAPS is a wholly owned subsidiary of Bank of Baroda which has its various subsidiaries engaged in the businesses of stock broking, lending, asset management, life insurance, health insurance and wealth management, among others.

BOBCAPS's activities have neither been suspended nor has it defaulted with any stock exchange authority with whom it has been registered in the last five years. BOBCAPS has not been debarred from doing business by any stock exchange or SEBI or any other authority. No disciplinary action has been taken by any regulatory authority against BOBCAPS affecting its equity research analysis activities.

BOBCAPS has obtained registration as a Research Entity under SEBI (Research Analysts) Regulations, 2014, having registration No.: INH000000040 valid till 03 February 2025. BOBCAPS is also a SEBI-registered intermediary for the broking business having SEBI Single Registration Certificate No.: INZ000159332 dated 20 November 2017.

BOBCAPS prohibits its analysts, persons reporting to analysts, and members of their households from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. Additionally, BOBCAPS prohibits its analysts and persons reporting to analysts from serving as an officer, director, or advisory board member of any companies that the analysts cover.

Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients that reflect opinions contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest. Additionally, other important information regarding our relationships with the company or companies that are the subject of this material is provided herein.

This material should not be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. We are not soliciting any action based on this material. It is for the general information of BOBCAPS's clients. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. Before acting on any advice or recommendation in this material, clients should consider whether it is suitable for their particular circumstances and, if necessary, seek professional advice.

The price and value of the investments referred to in this material and the income from them may go down as well as up, and investors may realize losses on any investments. Past performance is not a guide for future performance, future returns are not guaranteed and a loss of original capital may occur. BOBCAPS does not provide tax advice to its clients, and all investors are strongly advised to consult with their tax advisers regarding any potential investment in certain transactions — including those involving futures, options, and other derivatives as well as non-investment-grade securities — that give rise to substantial risk and are not suitable for all investors. The material is based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied on as such. Opinions expressed are our current opinions as of the date appearing on this material only. We endeavour to update on a reasonable basis the information discussed in this material, but regulatory, compliance, or other reasons may prevent us from doing so.

We and our affiliates, officers, directors, and employees, including persons involved in the preparation or issuance of this material, may from time to time have “long” or “short” positions in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein and may from time to time add to or dispose of any such securities (or investment). We and our affiliates may act as market makers or assume an underwriting commitment in the securities of companies discussed in this document (or in related investments), may sell them to or buy them from customers on a principal basis, and may also perform or seek to perform investment banking or advisory services for or relating to these companies and may also be represented in the supervisory board or any other committee of these companies.

For the purpose of calculating whether BOBCAPS and its affiliates hold, beneficially own, or control, including the right to vote for directors, one per cent or more of the equity shares of the subject company, the holdings of the issuer of the research report is also included.

BOBCAPS and its non-US affiliates may, to the extent permissible under applicable laws, have acted on or used this research to the extent that it relates to non-US issuers, prior to or immediately following its publication. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of or income derived from the investment. In addition, investors in securities such as ADRs, the value of which are influenced by foreign currencies, effectively assume currency risk. In addition, options involve risks and are not suitable for all investors. Please ensure that you have read and understood the Risk disclosure document before entering into any derivative transactions.

In the US, this material is only for Qualified Institutional Buyers as defined under rule 144(a) of the Securities Act, 1933. No part of this document may be distributed in Canada or used by private customers in the United Kingdom.

No part of this material may be (1) copied, photocopied, or duplicated in any form by any means or (2) redistributed without BOBCAPS's prior written consent.

Company-specific disclosures under SEBI (Research Analysts) Regulations, 2014

The research analyst(s) or his/her relatives do not have any material conflict of interest at the time of publication of this research report.

BOBCAPS or its research analyst(s) or his/her relatives do not have any financial interest in the subject company. BOBCAPS or its research analyst(s) or his/her relatives do not have actual/beneficial ownership of one per cent or more securities in the subject company at the end of the month immediately preceding the date of publication of this report.

The research analyst(s) has not received any compensation from the subject company in the past 12 months. Compensation of the research analyst(s) is not based on any specific merchant banking, investment banking or brokerage service transactions.

BOBCAPS or its research analyst(s) is not engaged in any market making activities for the subject company.

The research analyst(s) has not served as an officer, director or employee of the subject company.

BOBCAPS or its associates may have material conflict of interest at the time of publication of this research report.

BOBCAPS's associates may have financial interest in the subject company. BOBCAPS's associates may hold actual / beneficial ownership of one per cent or more securities in the subject company at the end of the month immediately preceding the date of publication of this report.

BOBCAPS or its associates may have managed or co-managed a public offering of securities for the subject company or may have been mandated by the subject company for any other assignment in the past 12 months.

BOBCAPS may have received compensation from the subject company in the past 12 months. BOBCAPS may from time to time solicit or perform investment banking services for the subject company. BOBCAPS or its associates may have received compensation from the subject company in the past 12 months for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory services in a merger or specific transaction. BOBCAPS or its associates may have received compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past 12 months.