

Company update

Pharmaceuticals

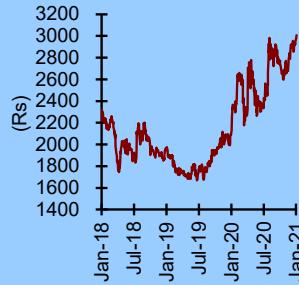
Target price Rs3,566

Shareholding pattern

	Mar '20	Jun '20	Sep '20
Promoters	65.9	62.4	62.4
Institutional investors	15.3	15.5	16.8
MFs and others	8.6	7.9	7.7
Fls/Banks/Ins.	2.7	3.7	4.8
FII	4.0	3.9	4.3
Others	18.8	22.1	20.8

Source: BSE India

Price chart



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INDIA

Alkem Laboratories

BUY

Maintained

Rs3,006

Pick-up starts in acute portfolio

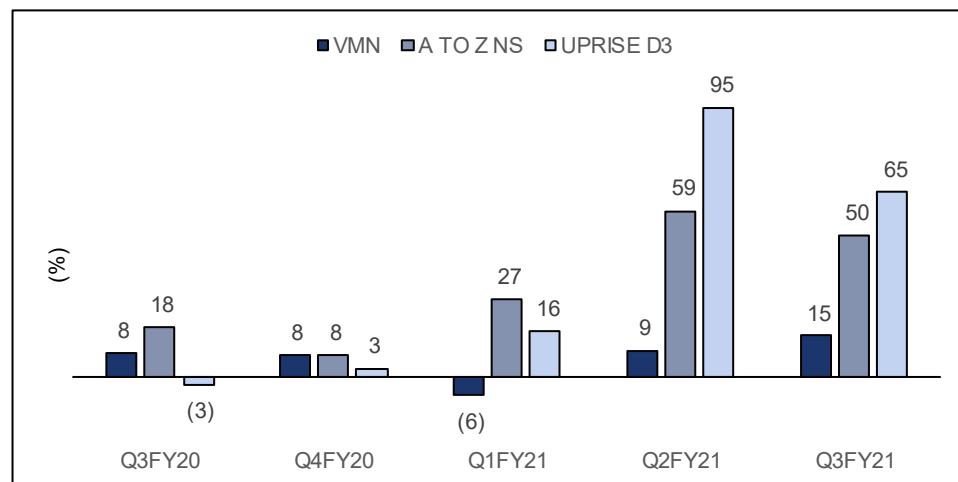
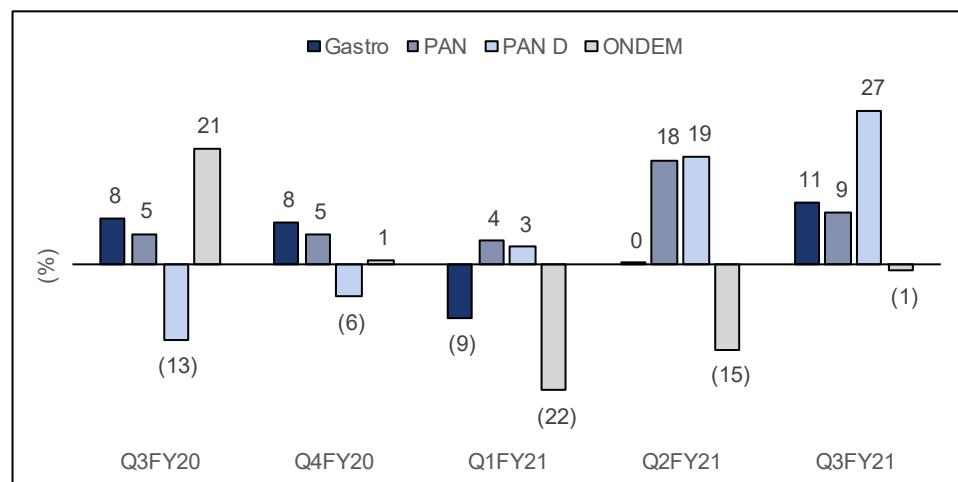
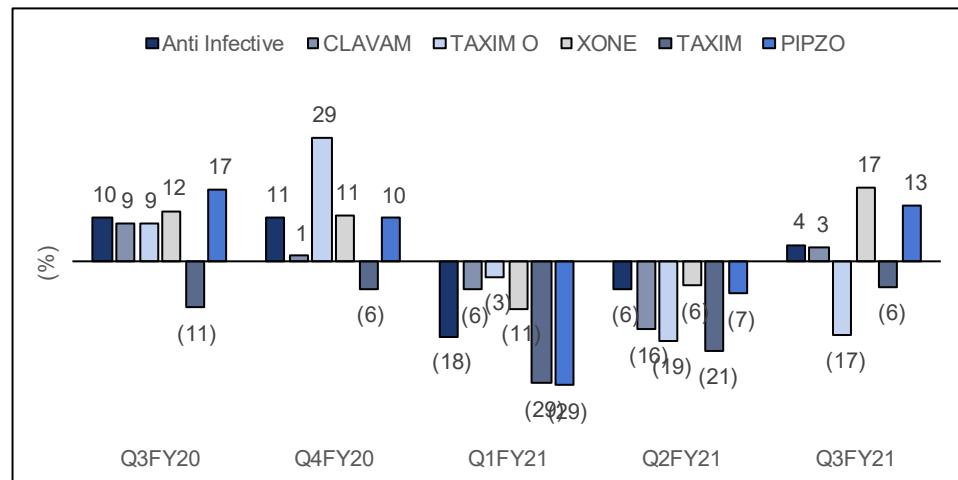
Alkem Laboratories' (Alkem) has underperformed BSE Healthcare Index in the last one year mainly due to acute heavy portfolio which was impacted by COVID-19. In our view, this temporary impact on acute portfolio caused by the lockdown has already been captured in the stock's underperformance. However, as per AIOCD (secondary sales) data, anti-infectives and gastro-intestinal, the two largest therapeutic segments for Alkem, have witnessed healthy ramp-up in growth. Additionally, growth in FY22E may hold room for some positive surprise considering the low base of FY21. We remain positive on the long-term outlook based on sustainable growth in the domestic market and continuous scale-up in US generic business coupled with an improving margin profile. Reiterate Buy.

- **Expect valuations to improve with ramp-up in growth:** The stock price underperformance over the last one year has been primarily due to weak growth resulting from lockdown, which in our view, is temporary and does not have any structural or fundamental impact on the company's business. Alkem, relative to its peers, was more severely impacted as its product mix is dominated by the acute portfolio. However, growth turned positive in Sep'20 and recovered well in Q3FY21 as per AIOCD (secondary sales) data. Further, the company's top brands – Pan, Pan D, etc. have outperformed the respective segments indicating faster recovery, which would also lead to margin improvement.
- **Recovery to continue in India business:** India formulations business contributes ~67% of total revenues and Alkem has consistently outperformed industry growth over the years. However, FY21 is likely to be an underperforming year for Alkem due to high dependence on acute portfolio. However, we expect growth to recover from Q3FY21 and reach double-digit Q4FY21 onwards. Additionally, growth in FY22E may hold room for some positive surprise considering the low base of FY21. We estimate 3.5% growth in Alkem's India business in FY21E and ~12% growth in FY22E and FY23E each. We believe, cost savings witnessed in H1FY21 would be partially sustainable and benefit Alkem more vs peers given its higher proportion of India sales.
- **Outlook:** We expect Alkem to register 9.4% revenue and 15.7% PAT CAGRs over FY20-FY23E with margin expansion of 350bps to 21.2%. We expect EBITDA margin to rebase at 20%+ for Alkem vs ~17% earlier. Strong earnings growth coupled with reduced capex would aid free cashflow generation of ~Rs40bn over FY21E-FY23E. It would also drive RoE/RoCE higher to 19.6%/18.1% respectively by FY23E.
- **Valuation and risks:** We remain positive on Alkem considering strong India business model, growth recovery and improving margin profile. We maintain Alkem as one of our top picks and reiterate **BUY** with a target price of Rs3,566/share based on 26xSep'22E EPS. Key downside risks: regulatory hurdles and delay in product approvals in the US.

Market Cap	Rs360bn/US\$4.9bn
Reuters/Bloomberg	ALKE.BO/ALKEM IN
Shares Outstanding (mn)	119.6
52-week Range (Rs)	3008/2117
Free Float (%)	37.6
FII (%)	4.3
Daily Volume (USD/'000)	7,236
Absolute Return 3m (%)	10.1
Absolute Return 12m (%)	43.4
Sensex Return 3m (%)	20.8
Sensex Return 12m (%)	19.1

Year to Mar	FY20	FY21E	FY22E	FY23E
Revenue (Rs mn)	83,444	90,118	99,355	109,188
Net Income (Rs mn)	10,957	14,738	15,359	17,435
EPS (Rs)	94.3	123.3	128.5	145.8
% Chg YoY	48.2	30.8	4.2	13.5
P/E (x)	31.9	24.4	23.4	20.6
CEPS (Rs)	115.4	146.7	153.0	172.1
EV/E (x)	24.7	17.6	16.7	14.7
Dividend Yield (%)	0.8	1.0	1.1	1.2
RoCE (%)	15.9	18.1	17.3	18.1
RoE (%)	19.4	22.1	19.9	19.6

Chart 1: Alkem's top products YoY growth against the respective industry



Source: Company data, I-Sec research

Valuations

We expect Alkem to witness an earnings CAGR of 15.7% over FY20-FY23E driven by revenue CAGR of 9.4% and EBITDA margin expansion to 21.2% in FY23E from 17.7% in FY20. Return ratios (RoE and RoCE) would improve with margin expansion led by strong growth in India. The stock currently trades at valuations of 23.4xFY22E and 20.6xFY23E earnings and EV/EBITDA multiple of 16.7xFY22E and 14.7xFY23E. We remain positive on the long-term outlook considering the company's strong brand presence in the domestic market with sustainable growth and scale-up of US generic business (56 pending ANDAs). We maintain **BUY** on the stock with a target price of Rs3,566/share based on 26xSep'22E earnings.

Chart 2: 1-year forward P/E



Source: Company data, I-Sec research

Summary financials (consolidated)

Table 1: Profit & Loss statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Domestic	54,540	56,474	63,432	70,758
Exports	27,379	32,199	34,456	36,940
Total Gross Sales	81,920	88,673	97,888	107,698
Excise	-	-	-	-
Other Operating Income	1,524	1,446	1,467	1,490
Total Net Revenue	83,444	90,118	99,355	109,188
YoY Growth%	13.4	8.0	10.2	9.9
Total Op. Exp.	68,710	69,944	78,552	86,036
EBITDA	14,734	20,174	20,803	23,152
Margins %	17.7	22.4	20.9	21.2
YoY Growth%	31.6	36.9	3.1	11.3
Depreciation	2,528	2,796	2,933	3,138
EBIT	12,206	17,379	17,870	20,014
Other Income	1,042	1,146	1,261	1,450
Interest	651	715	470	190
EO Items	-	-	-	-
PBT	12,598	17,810	18,661	21,274
Tax	1,419	2,850	3,079	3,617
Tax Rate (%)	11.3	16.0	16.5	17.0
Minority Interest	222	222	222	222
Reported PAT	10,957	14,738	15,359	17,435
Adj. PAT	10,957	14,738	15,359	17,435
Net Margins (%)	13.1	16.4	15.5	16.0

Source: Company data, I-Sec research

Table 2: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Paid-up Capital	239	239	239	239
Reserves & Surplus	61,368	71,667	82,399	94,583
Total Equity	61,607	71,906	82,639	94,822
Minority Interest	1,483	1,705	1,928	2,150
Total Debt	17,009	12,039	7,081	626
Deferred Liabilities	(9,326)	(9,326)	(9,326)	(9,326)
Capital Employed	70,773	76,324	82,322	88,273
Current Liabilities	19,335	20,532	22,673	24,809
Total Liabilities	90,108	96,856	104,995	113,082
Net Fixed Assets	32,710	33,414	34,481	35,343
Investments	915	988	1,089	1,197
Inventory	18,188	18,515	20,793	22,775
Debtors	16,494	17,813	19,639	21,582
Other Current Assets	9,180	9,900	10,896	11,956
Cash and Equivalents	12,621	16,226	18,096	20,228
Total Cur. Assets	57,398	63,442	70,514	77,739
Total Assets	90,108	96,856	104,995	113,082

Source: Company data, I-Sec research

Table 3: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
PBT (Adj. for Extraordinary)	12,598	17,810	18,661	21,274
Depreciation	2,528	2,796	2,933	3,138
Net Chg in WC	(5,429)	(1,197)	(2,996)	(2,889)
Taxes	(2,834)	(2,850)	(3,079)	(3,617)
Others	(1,662)	27	38	40
CFO	5,200	16,587	15,556	17,947
Capex	(3,476)	(3,500)	(4,000)	(4,000)
Net Investments made	(4,454)	(73)	(101)	(108)
Others	517	-	-	-
CFI	(7,414)	(3,573)	(4,101)	(4,108)
Change in Share capital	-	-	-	-
Change in Debts	5,838	(4,970)	(4,958)	(6,455)
Div. & Div Tax	(4,396)	(4,439)	(4,627)	(5,252)
Others	5,077	-	-	-
CFF	6,519	(9,409)	(9,584)	(11,707)
Total Cash Generated	4,306	3,605	1,871	2,132
Cash Opening Balance	6,616	10,922	14,527	16,398
Cash Closing Balance	10,922	14,527	16,398	18,530

Source: Company data, I-Sec research

Table 4: Key ratios

(Year ending March 31)

	FY20	FY21E	FY22E	FY23E
Adj EPS	94.3	123.3	128.5	145.8
YoY Growth%	48.2	30.8	4.2	13.5
Cash EPS	115.4	146.7	153.0	172.1
EBITDA - Core (%)	17.7	22.4	20.9	21.2
NPM (%)	13.1	16.4	15.5	16.0
Net Debt to Equity (x)	0.1	(0.1)	(0.1)	(0.2)
P/E (x)	31.9	24.4	23.4	20.6
EV/EBITDA Core (x)	24.7	17.6	16.7	14.7
P/BV (x)	5.7	4.9	4.2	3.7
EV/Sales (x)	4.4	3.9	3.5	3.1
RoCE (%)	15.9	18.1	17.3	18.1
RoE (%)	19.4	22.1	19.9	19.6
RoIC (%)	16.1	18.5	18.3	19.4
Book Value (Rs)	515	601	691	793
DPS (Rs)	23.6	30.8	32.1	36.5
Dividend Payout (%)	25.0	25.0	25.0	25.0
Div Yield (%)	0.8	1.0	1.1	1.2
Asset Turnover Ratio	1.0	1.0	1.0	1.0
Avg Collection days	63	69	69	69
Avg Inventory days	73	74	72	73

Source: Company data, I-Sec research

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