

BUY

TP: Rs 1,730 | ▲ 14%

AJANTA PHARMA

Pharmaceuticals

30 July 2020

Solid beat on margins – set to normalise in coming quarters

Ajanta Pharma (AJP) posted Q1 revenue/EBITDA growth of 9%/33% YoY to Rs 6.7bn/Rs 2.2bn. EBITDA margin expanded both YoY and QoQ to 33.4% due to higher gross margins and temporary reduction in SGA spends (lower travel/promotional costs amid lockdown). US and branded Africa sales were a beat while India/Asia was in line. Reported PAT stood at Rs 1.5bn. AJP is guiding for healthy operating leverage starting Q3. We retain BUY and roll over to a higher TP of Rs 1,730 (earlier Rs 1,650), based on 16x Sep'22E EV/EBITDA.

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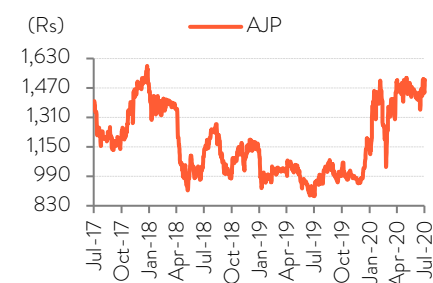
US/Africa branded sales beat estimates; India/Asia in line: India sales declined 10% YoY due to the Covid-19 impact on the acute portfolio, especially in dermatology and ophthalmology (guided to recover from Q3 onward). In export formulations, branded Africa/Asia sales grew at a healthy 17%/28% YoY. We continue to see good visibility in exports with two blocks operationalised in Q4. US sales were at US\$ 20mn (flat QoQ) despite the Ranitidine recall.

Ticker/Price	AJP IN/Rs 1,512
Market cap	US\$ 1.8bn
Shares o/s	88mn
3M ADV	US\$ 3.8mn
52wk high/low	Rs 1,580/Rs 825
Promoter/FPI/DII	71%/9%/9%

Source: NSE

EBITDA margin beat partly sustainable: Q1 gross margin surged 3ppt QoQ to 77% and includes positive forex impact of 1.5ppt. Also, SGA/R&D cost fell 12%/23% YoY due to lower activity during the Covid lockdown. This led to a strong EBITDA margin of 33.4% (24.8% est.). Margins would moderate from Q2 as lockdown restrictions ease and travel/promotional spends normalise.

STOCK PERFORMANCE



Retain BUY: We expect a stable brand franchise (India and EM), US operating leverage and capex moderation to drive a 15%+ EPS CAGR for AJP over FY20-FY23. With over 75% of FY21/FY22 EPS estimated to accrue from the branded business, improving FCF and 30%+ ROIC beyond FY22E, the stock has scope for valuation upsides. We marginally tweak FY21/FY22 EPS estimates on higher tax guidance of 28% (vs. 26% earlier) and roll forward to a TP of Rs 1,730.

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	20,553	25,878	27,680	31,375	35,364
EBITDA (Rs mn)	5,653	6,944	7,437	8,676	10,029
Adj. net profit (Rs mn)	3,869	4,082	4,767	5,981	7,263
Adj. EPS (Rs)	44.1	46.6	54.4	68.2	82.8
Adj. EPS growth (%)	(17.4)	5.5	16.8	25.5	21.4
Adj. ROAE (%)	17.8	16.6	16.7	18.2	19.1
Adj. P/E (x)	34.3	32.5	27.8	22.2	18.3
EV/EBITDA (x)	23.3	19.0	17.7	15.0	12.8

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)	Q1FY21E	Var. (%)	FY20	FY19
Net Sales	6,682	6,119	9.2	6,820	(2.0)	6,100	9.5	25,878	20,552
EBITDA	2,235	1,685	32.6	1,664	34.3	1,511	47.9	6,988	5,586
Depreciation	280	227	-	260	-	270	-	956	721
EBIT	1,955	1,458	34.1	1,404	39.2	1,241	-	6,032	4,865
Interest	16	18	-	36	-	30	-	119	12
Other Income	131	76	-	116	-	90	-	470	293
PBT	2,070	1,516	36.5	1,484	39.4	1,301	59.1	6,384	5,146
Less: Taxation	589	368	-	470	-	338	-	1,964	1,271
Less: Minority Interest	-	-	-	-	-	-	-	0	0
Recurring PAT	1,481	1,148	29.0	1,014	46.0	963	53.8	4,420	3,875
Exceptional items	0	0	-	275	-	0	-	261	0
Reported PAT	1,481	1,148	29.0	1,289	14.8	963	53.8	4,681	3,875
Key Ratios (%)									
Gross Margin	77.1	76.7	-	74.0	-	74.5	-	74.7	81.4
EBITDA Margin	33.4	27.5	-	24.4	-	24.8	-	27.0	27.2
Tax / PBT	28.5	24.3	-	31.7	-	26.0	-	30.8	24.7
NPM	22.2	18.8	-	14.9	-	15.8	-	17.1	18.9
EPS (Rs)	16.9	13.1	-	11.6	-	11.0	-	50.4	44.2

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)	Q1FY21E	Var. (%)	FY20	FY19
Domestic Formulation	1,740	1,940	(10.3)	1,770	(1.7)	1,724	0.9	7,690	6,900
Export Formulation	4,800	4,040	18.8	4,900	(2.0)	4,256	12.8	17,890	13,250
Africa	1,700	1,730	(1.7)	1,380	23.2	1,412	20.4	5,950	5,020
Asia	1,610	1,260	27.8	2,090	(23.0)	1,512	6.5	6,740	5,280
US	1,490	1,020	46.1	1,430	4.2	1,332	11.9	5,150	2,830
Others/LATAM	-	30	(100.0)	0	-	-	-	50	120
Other Op Income	142	76	86.8	150	(5.3)	120	18	504	382
Revenues	6,682	6,056	10.3	6,820	(2.0)	6,100	9.5	26,084	20,532

Source: Company, BOBCAPS Research

Valuation methodology

AJP has a strong track record in terms of rational capital allocation, building a brand franchise, flawless cGMP compliance and stable returns ratios. We believe the branded generic franchise (India and EM) is strong and likely to remain resilient – this alongside operating leverage in the US business should drive an accelerated 15%+ EPS CAGR over FY20-FY23 (vs. flat growth for FY18-FY20).

In FY18, the company embarked on a major capex drive worth Rs 11bn towards augmenting formulation capacity, which is now nearing an end and should fuel a doubling of current sales, per management. We expect improved FCF momentum over the next 2-3 years based on healthy earnings growth and a normalised capex run-rate of Rs 1bn annually. ROIC levels are thus forecast to expand from 26% in FY20 to 33% by FY23.

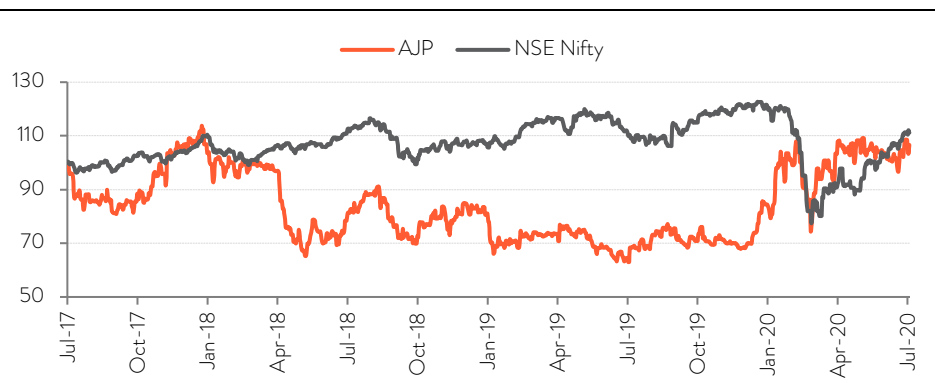
We marginally cut our FY21/FY22 EPS estimates by 3%/1% to factor in higher tax guidance at 28%. At CMP, the stock is trading at 15x FY22E EBITDA (15% below the five-year mean) and 22x P/E which looks attractive in the context of ROIC improvement. We retain BUY and roll forward to a Sep'21 target price of Rs 1,730 (from Rs 1,650), based on an unchanged 16x one-year forward EV/EBITDA multiple (23x implied P/E).

FIG 3 – REVISED ESTIMATES

(Rs bn)	New			Old			Change (%)		
	FY20A	FY21E	FY22E	FY20P	FY21E	FY22E	FY20E	FY21E	FY22E
Sales	25.9	27.7	31.4	26.2	27.7	31.3	(1.1)	0.0	0.1
EBITDA	6.9	7.4	8.7	7.0	7.4	8.6	(0.7)	0.7	0.9
EBITDA margin (%)	26.8	26.9	27.7	26.7	26.7	27.4	12bps	18bps	20bps
EPS (Rs)	47	54	68	50	56	69	(7.4)	(3.0)	(1.1)

Source: Company, BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Concentration and regulatory risk in India business:** AJP's domestic formulation business is concentrated around three key therapies – ophthalmology, cardiology and dermatology – which drive 90% of sales. Any adverse regulatory action here can slow down overall business momentum. Current portfolio under price control is at 13% of India sales vs. 16% for industry.
- **US execution:** We estimate that the US business will contribute a third of our EPS over the next three years. This is mainly dependent on two key units – Paithan (~90% of existing US sales) and Dahej (future growth driver). Establishment inspection reports (EIR) for both units are in place (last inspected in Jul-Aug'19). Thus, strong cGMP compliance is key.
- **Slower offtake in branded generic exports:** Currency devaluation and repatriation concerns will lead to slower growth in branded generics markets.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	20,553	25,878	27,680	31,375	35,364
EBITDA	5,653	6,944	7,437	8,676	10,029
Depreciation	720	957	1,104	1,181	1,264
EBIT	4,933	5,987	6,332	7,495	8,765
Net interest income/(expenses)	(12)	(119)	(52)	(78)	(78)
Other income/(expenses)	210	176	341	558	871
Exceptional items	0	0	0	0	0
EBT	5,132	6,044	6,621	7,975	9,557
Income taxes	1,263	1,962	1,854	1,994	2,294
Extraordinary items	0	595	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	3,869	4,677	4,767	5,981	7,263
Adjustments	0	595	0	0	0
Adjusted net profit	3,869	4,082	4,767	5,981	7,263

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	2,252	3,622	3,033	3,438	3,875
Other current liabilities	944	1,831	1,384	1,569	1,768
Provisions	383	246	263	298	336
Debt funds	340	436	1,300	1,300	1,300
Other liabilities	0	0	0	0	0
Equity capital	175	175	175	175	175
Reserves & surplus	22,545	26,398	30,212	34,996	40,807
Shareholders' fund	22,721	26,573	30,387	35,172	40,983
Total liabilities and equities	26,640	32,708	36,368	41,777	48,262
Cash and cash eq.	1,004	2,049	4,083	7,256	11,328
Accounts receivables	4,594	7,753	6,825	7,736	8,720
Inventories	4,357	4,956	5,688	6,447	7,267
Other current assets	1,510	1,211	2,214	2,510	2,829
Investments	776	794	794	794	794
Net fixed assets	11,719	14,509	14,763	15,034	15,324
CWIP	2,613	1,318	2,000	2,000	2,000
Intangible assets	67	117	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	26,640	32,707	36,368	41,777	48,262

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	4,589	5,634	5,871	7,162	8,528
Interest expenses	12	119	52	78	78
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(186)	(1,339)	(1,826)	(1,341)	(1,448)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	4,414	4,415	4,098	5,899	7,158
Capital expenditures	(1,930)	(3,294)	(1,358)	(1,453)	(1,555)
Change in investments	1,123	(18)	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(807)	(3,313)	(1,358)	(1,453)	(1,555)
Equities issued/Others	(2)	0	0	0	0
Debt raised/repaid	330	96	865	0	0
Interest expenses	(12)	(119)	(52)	(78)	(78)
Dividends paid	(795)	(816)	(953)	(1,196)	(1,453)
Other financing cash flows	(3,055)	783	(565)	0	0
Cash flow from financing	(3,533)	(57)	(706)	(1,274)	(1,531)
Changes in cash and cash eq.	74	1,045	2,034	3,172	4,073
Closing cash and cash eq.	1,004	2,049	4,083	7,256	11,328

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	44.1	53.3	54.4	68.2	82.8
Adjusted EPS	44.1	46.6	54.4	68.2	82.8
Dividend per share	9.0	9.3	10.9	13.6	16.6
Book value per share	259.1	303.0	346.5	401.0	467.3

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	6.4	5.1	4.8	4.2	3.6
EV/EBITDA	23.3	19.0	17.7	15.0	12.8
Adjusted P/E	34.3	32.5	27.8	22.2	18.3
P/BV	5.8	5.0	4.4	3.8	3.2

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	75.4	67.5	72.0	75.0	76.0
Interest burden (PBT/EBIT)	104.0	101.0	104.6	106.4	109.0
EBIT margin (EBIT/Revenue)	24.0	23.1	22.9	23.9	24.8
Asset turnover (Revenue/Avg TA)	23.5	25.8	23.6	23.0	22.5
Leverage (Avg TA/Avg Equity)	1.0	1.0	1.0	1.0	1.0
Adjusted ROAE	17.8	16.6	16.7	18.2	19.1

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	(3.6)	25.9	7.0	13.3	12.7
EBITDA	(14.1)	22.8	7.1	16.7	15.6
Adjusted EPS	(17.4)	5.5	16.8	25.5	21.4
Profitability & Return ratios (%)					
EBITDA margin	27.5	26.8	26.9	27.7	28.4
EBIT margin	24.0	23.1	22.9	23.9	24.8
Adjusted profit margin	18.8	15.8	17.2	19.1	20.5
Adjusted ROAE	17.8	16.6	16.7	18.2	19.1
ROCE	23.5	24.6	22.7	23.6	24.5
Working capital days (days)					
Receivables	82	109	90	90	90
Inventory	77	70	75	75	75
Payables	40	51	40	40	40
Ratios (x)					
Gross asset turnover	1.3	1.3	1.3	1.4	1.5
Current ratio	3.2	2.8	4.0	4.5	5.0
Net interest coverage ratio	425.3	50.3	121.6	96.1	112.4
Adjusted debt/equity	0.0	(0.1)	(0.1)	(0.2)	(0.2)

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

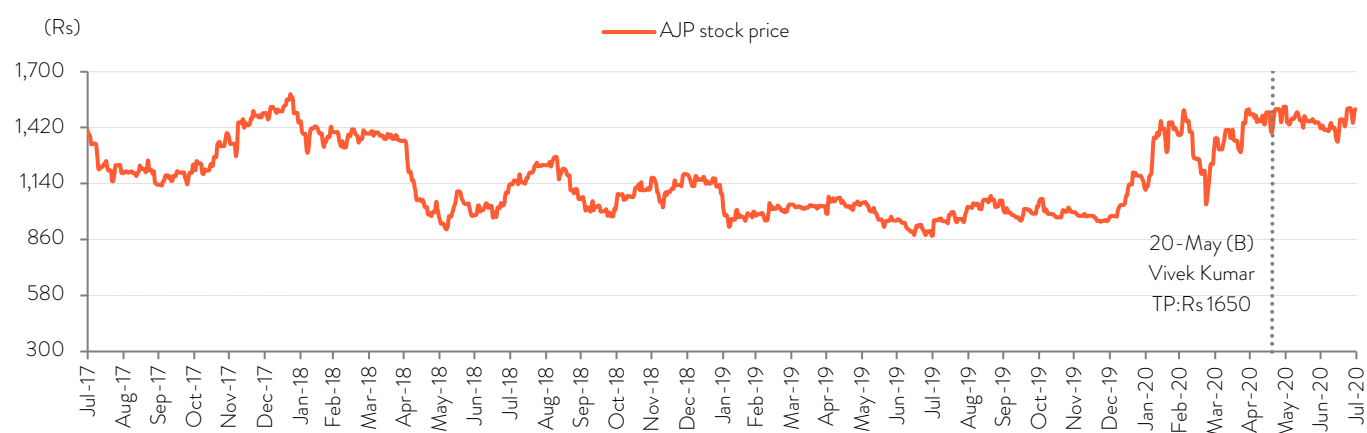
ADD – Expected return from >+5% to +15%

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)

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

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