

BUY

TP: Rs 2,750 | ▲ 20%

AJANTA PHARMA

Pharmaceuticals

31 July 2021

Strong earnings growth; reiterate BUY

- Q1 PAT robust at Rs 1.7bn, up 17% YoY. Sales grew 12% YoY while EBITDA declined 2%
- Gross margin steady at 77% on a favourable product mix; higher R&D and staff cost drove 400bps YoY drop in EBITDA margin to 29.4%
- We raise FY22-FY23 EPS 4-5% and roll forward to a Jun'22 TP of Rs 2,750 (vs. Rs 2,300); maintain BUY

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Robust India growth: AJP's India sales grew 32% YoY (+5% QoQ) in Q1FY22 backed by a strong uptick in all its therapies owing to higher promotional activity. In export formulations, the company grew 12.8% YoY in the US, 4.1% in Africa and 2.5% in Asia. US sales totalled US\$ 23mn (-4% QoQ).

Stable gross margin; higher R&D and staff cost hurt EBITDA margin: A better product mix in favour of domestic formulations supported a stable Q1 gross margin of 77%. EBITDA margin contracted 400bps YoY and 485bps QoQ to 29.4% due to higher R&D spend at 6% of revenue (vs. 5.2%/4.6% in Q4FY21/Q1FY21) and higher staff cost at 21.1% of revenue (vs. 19.3%/20.3%).

Earnings call highlights: (1) Management lowered the FY22 tax guidance to 22% vs. earlier expectations of 26-27%. (2) Capex to be around Rs 2bn in FY22, with current capacity adequate for the next three years, implying that only maintenance capex will be required going forward. (3) The company launched five products in India and one in the US in Q1. It plans to have 3-4 launches in the US market in FY22.

Estimates and target price raised: We raise our FY22-FY23 EPS estimates by 4-5% on lower tax guidance. Based on sustained gross margins, improving domestic business and expected higher ANDA filings in the US (10+ p.a.), we upgrade our target one-year forward EV/EBITDA multiple from 16x to 19x – a 25% premium to the stock's eight-year mean, which translates to an implied P/E of 26x. On rollover, we have a new Jun'22 TP of 2,750 (vs. Rs 2,300).

Reiterate BUY: Shares of AJP have advanced 25% since 1 May 2021 and are currently trading at 16.4x one-year forward EV/EBITDA and 22.2x P/E. We find valuations attractive given that the company's stable brand franchise (India/EM), US operating leverage, lower tax burden and capex moderation are likely to drive a brisk 15% EPS CAGR over FY21-FY24. Further, improving FCF, 38%+ ROIC beyond FY24E and a steady pace of new launches (21 brands launched in India in FY21) should support stock upsides. Reiterate BUY.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	AJP IN/Rs 2,292
Market cap	US\$ 2.7bn
Free float	30%
3M ADV	US\$ 3.4mn
52wk high/low	Rs 2,435/Rs 1,425
Promoter/FPI/DII	70%/9%/12%

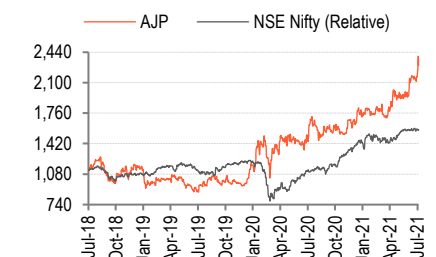
Source: NSE | Price as of 30 Jul 2021

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	28,897	33,007	37,456
EBITDA (Rs mn)	9,990	10,108	11,834
Adj. net profit (Rs mn)	6,534	7,313	8,824
Adj. EPS (Rs)	74.5	83.4	100.6
Consensus EPS (Rs)	74.5	83.8	99.8
Adj. ROAE (%)	22.9	22.0	22.2
Adj. P/E (x)	30.8	27.5	22.8
EV/EBITDA (x)	19.8	19.5	16.6
Adj. EPS growth (%)	38.5	11.9	20.7

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)
Net Sales	7,480	6,682	11.9	7,568	(1.2)
EBITDA	2,202	2,235	(1.5)	2,594	(15.1)
Depreciation	309	280	-	306	-
EBIT	1,893	1,955	(3.2)	2,288	(17.3)
Interest	15	16	-	26	-
Other Income	326	131	-	25	-
PBT	2,205	2,070	6.5	2,288	(3.6)
Less: Taxation	467	589	-	695	-
Less: Minority Interest	-	-	-	-	-
Recurring PAT	1,738	1,481	17.3	1,593	9.1
Exceptional items	0	0	-	0	-
Reported PAT	1,738	1,481	17.3	1,593	9.1
Key Ratios (%)			(bps)		(bps)
Gross Margin	77.1	77.1	(5)	77.8	(76)
EBITDA Margin	29.4	33.4	(401)	34.3	(484)
Tax / PBT	21.2	28.5	-	30.4	-
NPM	23.2	22.2	-	21.0	-
EPS (Rs)	20.0	17.5	107	18.3	219

Source: Company, BOBCAPS Research

Fig 2 – Revenue mix

(Rs mn)	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)
Domestic Formulation	2,290	1,740	31.6	2,180	5.0
Exports Formulation	5,100	4,800	6.3	5,260	(3.0)
Africa	1,770	1,700	4.1	1,770	0.0
Asia	1,650	1,610	2.5	1,760	(6.3)
US	1,680	1,490	12.8	1,730	(2.9)
Other Op Income	90	142	(36.7)	128	(30.0)
Revenue	7,480	6,682	11.9	7,568	(1.2)
USDINR	74	74	-0.4	73	1.1
US revenue (US\$ mn)	23	20	13.2	24	(4.0)

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 robust and likely to remain resilient – this alongside operating leverage in the US business should drive a 15%+ EPS CAGR over FY21-FY24 (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-1.2bn annually. ROIC levels are thus forecast to improve north of 38% beyond FY24.

We increase our FY22/FY23 EPS estimates by 4-5% to factor in lower tax rate in the light of management guidance. Based on sustained gross margins, improving domestic business and higher ANDA filings, we upgrade our target one-year forward EV/EBITDA multiple from 16x to 19x – a 25% premium to the stock's eight-year mean, which translates to an implied 26x P/E. On rollover, we have a new Jun'22 TP of 2,750 (vs. Rs 2,300). The stock is currently trading at 16.4x one-year forward EV/EBITDA and 22.2x P/E, which looks attractive in the context of ROIC improvement. Retain BUY.

Fig 3 – Revised estimates

(Rs mn)	New			Old		Change (%)	
	FY22E	FY23E	FY24E	FY22E	FY23E	FY22E	FY23E
Sales	33	37	42	33	37	(0.0)	(0.0)
EBITDA	10	12	13	10	12	0.0	(0.0)
EBITDA Margin (%)	30.6	31.6	31.1	30.6	31.6	0bps	(0bps)
EPS (Rs)	84	101	113	80	97	5.3	4.4

Source: BOBCAPS Research

Fig 4 – Key assumptions

Parameter (Rs mn)	FY21	FY22E	FY23E	FY24E
India Formulation	8,130	9,239	10,426	11,770
Africa	6,745	7,149	7,592	8,081
Tender business	2,710	2,710	2,710	2,710
Branded business	4,035	4,439	4,882	5,371
Asia	7,159	8,302	9,398	10,640
US	6,370	7,579	9,206	10,977
Others	46	46	46	46
OOI	447	692	787	892

Source: Company, BOBCAPS Research

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. The 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 could lead to slower growth in branded generics markets.

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	25,878	28,897	33,007	37,456	42,406
EBITDA	6,833	9,990	10,108	11,834	13,187
Depreciation	957	1,161	1,207	1,303	1,386
EBIT	5,876	8,829	8,901	10,530	11,801
Net interest inc./(exp.)	(119)	(83)	(12)	(12)	(12)
Other inc./(exp.)	921	251	486	795	1,291
Exceptional items	0	0	0	0	0
EBT	6,678	8,997	9,375	11,313	13,080
Income taxes	1,962	2,463	2,063	2,489	3,139
Extraordinary items	39	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	4,756	6,534	7,313	8,824	9,941
Adjustments	39	0	0	0	0
Adjusted net profit	4,716	6,534	7,313	8,824	9,941

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	3,622	3,739	3,617	4,105	4,647
Other current liabilities	1,831	2,677	1,650	1,873	2,120
Provisions	246	296	339	384	435
Debt funds	436	198	198	198	198
Other liabilities	0	0	0	0	0
Equity capital	175	174	174	174	174
Reserves & surplus	26,398	30,203	36,053	43,112	51,082
Shareholders' fund	26,573	30,377	36,227	43,286	51,256
Total liab. and equities	32,708	37,286	42,031	49,846	58,656
Cash and cash eq.	2,049	2,096	4,617	9,868	15,931
Accounts receivables	7,753	7,384	8,139	9,236	10,456
Inventories	4,956	7,665	6,782	7,696	8,714
Other current assets	1,211	1,891	2,641	2,996	3,392
Investments	794	1,846	1,846	1,846	1,846
Net fixed assets	14,509	15,214	16,007	16,204	16,318
CWIP	1,318	1,082	2,000	2,000	2,000
Intangible assets	117	108	0	0	0
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	32,707	37,286	42,031	49,846	58,656

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash flow from operations	4,414	5,770	6,805	8,528	9,546
Capital expenditures	(3,294)	(1,550)	(2,000)	(1,500)	(1,500)
Change in investments	(18)	(1,051)	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(3,313)	(2,601)	(2,000)	(1,500)	(1,500)
Equities issued/Others	0	(2)	0	0	0
Debt raised/repaid	96	(238)	0	0	0
Interest expenses	(119)	(83)	(12)	(12)	(12)
Dividends paid	(943)	(1,307)	(1,463)	(1,765)	(1,971)
Other financing cash flows	910	(1,493)	(810)	0	0
Cash flow from financing	(56)	(3,122)	(2,285)	(1,777)	(1,983)
Chg in cash & cash eq.	1,045	47	2,521	5,251	6,063
Closing cash & cash eq.	2,049	2,096	4,617	9,868	15,931

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	53.3	74.5	83.4	100.6	113.4
Adjusted EPS	53.8	74.5	83.4	100.6	113.4
Dividend per share	10.8	15.0	16.8	20.3	22.7
Book value per share	303.0	346.4	413.1	493.6	584.5

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	7.7	6.9	6.0	5.2	4.5
EV/EBITDA	29.0	19.8	19.5	16.6	14.6
Adjusted P/E	42.6	30.8	27.5	22.8	20.2
P/BV	7.6	6.6	5.5	4.6	3.9

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	70.6	72.6	78.0	78.0	76.0
Interest burden (PBT/EBIT)	113.6	101.9	105.3	107.4	110.8
EBIT margin (EBIT/Revenue)	22.7	30.6	27.0	28.1	27.8
Asset turnover (Rev./Avg TA)	25.8	25.1	24.6	23.4	22.3
Leverage (Avg TA/Avg Equity)	1.0	1.0	1.0	1.0	1.0
Adjusted ROAE	19.1	22.9	22.0	22.2	21.0

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	25.9	11.7	14.2	13.5	13.2
EBITDA	20.9	46.2	1.2	17.1	11.4
Adjusted EPS	21.9	38.5	11.9	20.7	12.7
Profitability & Return ratios (%)					
EBITDA margin	26.4	34.6	30.6	31.6	31.1
EBIT margin	22.7	30.6	27.0	28.1	27.8
Adjusted profit margin	18.2	22.6	22.2	23.6	23.4
Adjusted ROAE	19.1	22.9	22.0	22.2	21.0
ROCE	27.2	31.5	28.0	28.3	27.6
Working capital days (days)					
Receivables	109	93	90	90	90
Inventory	70	97	75	75	75
Payables	51	47	40	40	40
Ratios (x)					
Gross asset turnover	1.3	1.4	1.4	1.5	1.6
Current ratio	2.8	2.8	4.0	4.7	5.3
Net interest coverage ratio	49.4	106.8	750.4	887.7	994.8
Adjusted debt/equity	(0.1)	(0.1)	(0.1)	(0.2)	(0.3)

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

Disclaimer

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

BUY – Expected return >+15%

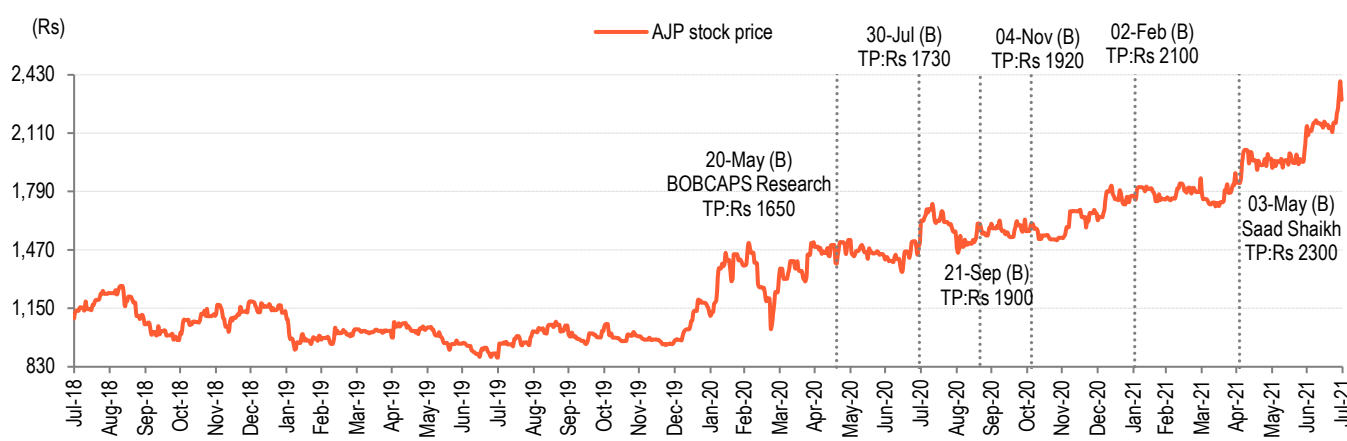
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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): AJANTA PHARMA (AJP IN)



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

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