

**HOLD**

TP: Rs 880 | ▲ 1%

**AUROBINDO PHARMA**

| Pharmaceuticals

| 15 August 2023

**Broad-based growth; lower to HOLD post rally**

- Q1 revenue/EBITDA beat consensus by 4%/9% with adj. PAT (ex-one-off charge) running 15% ahead
- EBITDA margin climbed 130bps YoY to 16.8%; guided to exceed 18% in FY24
- FY24-FY25 EBITDA estimates raised 11-12% and TP reset to Rs 880 (vs. Rs 635), but rating cut to HOLD post recent rally

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**Broad-based growth:** ARBP reported Q1FY24 revenue growth of 10% YoY to Rs 68.5bn with double-digit growth across businesses, except antiretroviral formulations which reported a 50% YoY decline. The company fared well in Europe (+19% YoY) due to market share gains as competitors struggled with shortages. The active pharma ingredient (API) business reported healthy 14% YoY growth on the back of improved demand.

**US price erosion has stabilised:** US business posted healthy revenue growth of 9% QoQ (+4% YoY) to US\$ 402mn as the business environment improved and price erosion stabilised. Per management, no one-off sales were recorded in Q1 and the company did not benefit from shortages arising from the plant disruption at Pfizer. ARBP plans to launch gRevlimid in the US market in October.

**FY24 margin guided at 18%+:** EBITDA increased 19% YoY to Rs 11.5bn accompanied by margin expansion of 130bps to 16.8% as better capacity utilisation raised operating leverage. Gross margin was flat YoY but fell 80bps QoQ on account of a product mix change and sequentially lower other operating income. Management guides for an EBITDA margin of over 18% in FY24, supported by the upcoming launch of gRevlimid, normalised export incentives and resumption of Puerto Rico operations (production halted for expansion).

**Valuations full; lower to HOLD:** Following the strong April-June quarter on the back of an improved business environment in the US and Europe and better margin guidance, we raise our FY24-FY25 EBITDA estimates by 11-12% and increase our FY25E EV/EBITDA multiple to 9x (from 7x) – in line with the 5Y average. Our TP thus rises to Rs 880 (from Rs 635). Even so, we downgrade our rating from BUY to HOLD as the stock has rallied ~45% in 3M and offers low upside potential at prevailing valuations of 10.2x/8.8x FY24E/FY25E EV/EBITDA.

**Key changes**

Target	Rating
▲	▼

Ticker/Price	ARBP IN/Rs 872
Market cap	US\$ 6.2bn
Free float	48%
3M ADV	US\$ 18.1mn
52wk high/low	Rs 888/Rs 397
Promoter/FPI/DII	52%/24%/16%

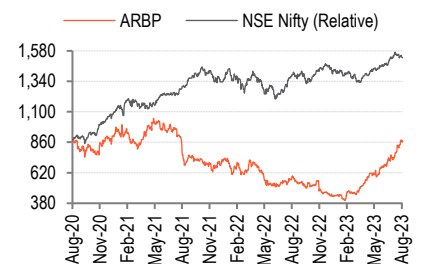
Source: NSE | Price as of 14 Aug 2023

**Key financials**

Y/E 31 Mar	FY23A	FY24E	FY25E
Total revenue (Rs mn)	2,48,554	2,71,092	2,91,396
EBITDA (Rs mn)	37,582	48,857	55,785
Adj. net profit (Rs mn)	20,018	29,031	32,710
Adj. EPS (Rs)	34.2	49.5	55.8
Consensus EPS (Rs)	34.2	46.0	54.3
Adj. ROAE (%)	7.8	10.4	10.7
Adj. P/E (x)	25.5	17.6	15.6
EV/EBITDA (x)	13.4	10.2	8.8
Adj. EPS growth (%)	(26.0)	45.0	12.7

Source: Company, Bloomberg, BOBCAPS Research

**Stock performance**



Source: NSE



**Fig 1 – Quarterly performance**

(Rs mn)	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)	FY23	FY22	YoY (%)
<b>Net Sales</b>	<b>68,505</b>	<b>62,359</b>	<b>9.9</b>	<b>64,730</b>	<b>5.8</b>	<b>2,48,554</b>	<b>2,34,555</b>	<b>6.0</b>
<b>EBITDA</b>	<b>11,514</b>	<b>9,647</b>	<b>19.4</b>	<b>10,022</b>	<b>14.9</b>	<b>37,582</b>	<b>43,868</b>	<b>(14.3)</b>
Depreciation	3,266	2,795	-	3,456	-	12,446	11,265	-
<b>EBIT</b>	<b>8,248</b>	<b>6,852</b>	<b>20.4</b>	<b>6,566</b>	<b>25.6</b>	<b>25,136</b>	<b>32,603</b>	<b>(22.9)</b>
Interest	566	146	-	556	-	1,405	486	-
Other Income	1,163	406	-	1,349	-	3,254	2,504	-
<b>PBT</b>	<b>8,846</b>	<b>7,112</b>	<b>24.4</b>	<b>7,359</b>	<b>20.2</b>	<b>26,985</b>	<b>34,620</b>	<b>(22.1)</b>
Less: Taxation	2,423	1,586	-	2,242	-	6,849	7,256	-
Less: Minority Interest	18	38	-	55	-	118	302	-
<b>Recurring PAT</b>	<b>6,405</b>	<b>5,488</b>	<b>16.7</b>	<b>5,063</b>	<b>26.5</b>	<b>20,018</b>	<b>27,062</b>	<b>(26.0)</b>
Exceptional items	(698)	(283)	-	0	-	(744)	(580)	-
<b>Reported PAT</b>	<b>5,708</b>	<b>5,205</b>	<b>9.7</b>	<b>5,063</b>	<b>12.7</b>	<b>19,275</b>	<b>26,482</b>	<b>(27.2)</b>
<b>Key Ratios (%)</b>			<b>(bps)</b>		<b>(bps)</b>			<b>(bps)</b>
Gross Margin	53.9	53.7	24	54.7	(77)	54.6	56.8	(220)
EBITDA Margin	16.8	15.5	134	15.5	132	15.1	18.7	(358)
Tax / PBT	27.4	22.3	-	30.5	-	25.4	21.0	-
NPM	9.3	8.8	-	7.8	-	8.1	11.5	-
EPS (Rs)	10.9	9.4	-	8.6	-	34.2	46.2	-

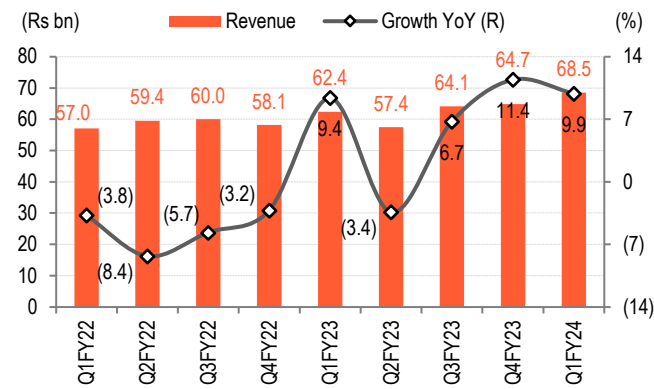
Source: Company, BOBCAPS Research

**Fig 2 – Revenue mix**

(Rs mn)	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)	FY23	FY22	YoY (%)
<b>Formulations</b>	<b>58,170</b>	<b>53,294</b>	<b>9.1</b>	<b>54,560</b>	<b>6.6</b>	<b>2,10,079</b>	<b>1,99,392</b>	<b>5.4</b>
US	33,040	29,711	11.2	30,450	8.5	1,16,549	1,11,221	4.8
Europe	18,370	15,481	18.7	16,600	10.7	64,255	64,802	(0.8)
EM	4,860	4,306	12.9	5,920	(17.9)	19,734	15,039	31.2
ARV	1,900	3,796	(49.9)	1,590	19.5	9,541	8,330	14.5
<b>APIs</b>	<b>10,330</b>	<b>9,065</b>	<b>14.0</b>	<b>10,180</b>	<b>1.5</b>	<b>38,485</b>	<b>35,154</b>	<b>9.5</b>
<b>Net Sales</b>	<b>68,500</b>	<b>62,359</b>	<b>9.8</b>	<b>64,740</b>	<b>5.8</b>	<b>2,48,564</b>	<b>2,34,546</b>	<b>6.0</b>
USDINR	82	77	6.7	82	(0.1)	80.2	74.4	7.8
US revenue (US\$ mn)	402	386	4.3	370	8.6	1453	1495	(2.8)

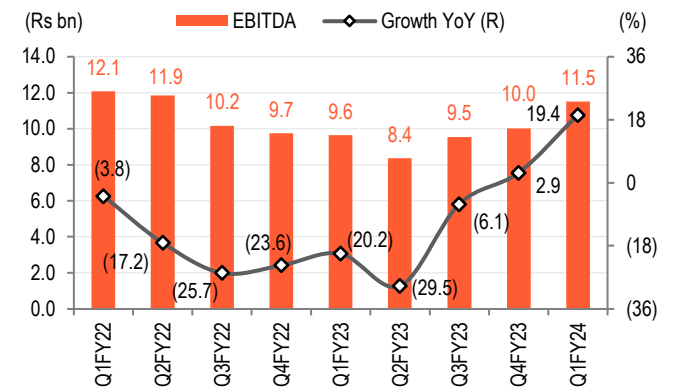
Source: Company, BOBCAPS Research

**Fig 3 – Revenue**



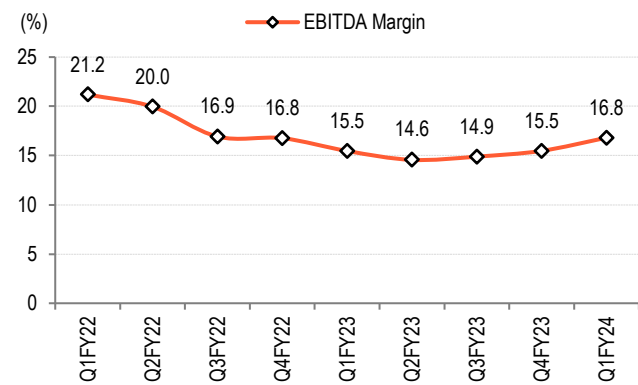
Source: Company, BOBCAPS Research

**Fig 4 – EBITDA**



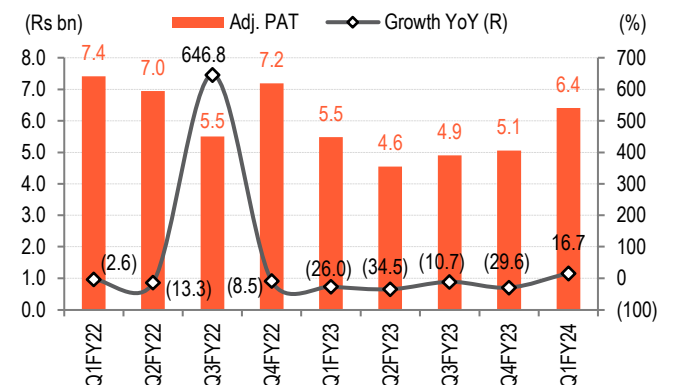
Source: Company, BOBCAPS Research

**Fig 5 – EBITDA margin**



Source: Company, BOBCAPS Research

**Fig 6 – Adj. PAT**



Source: Company, BOBCAPS Research

## Earnings call highlights

- **US:** ARBP posted strong revenue growth in the US business at 9% QoQ (+4% YoY) to US\$ 402mn in Q1FY24. No one-off sales were recorded during the quarter.
- **Eugia:** Eugia Pharma's revenue in the US, which includes generic injectables and specialty oral solid dosage (OSD) drugs, stood at US\$ 90.9mn in Q1 (22.6% of total US revenue). Of this, US\$ 80.1mn came from generic injectables. Global Eugia revenue on a proforma basis totalled US\$ 122mn in Q1. The board has approved business restructuring at Eugia.
- **Europe:** ARBP saw strong growth in Europe due to market share gains as competitors struggled with shortages. This also helped margins.
- **Emerging markets (EM):** EMs reported healthy growth of 13% YoY. Within this, domestic formulation sales stood at Rs 524mn (-1% QoQ) and production-linked incentives (PLI) at Rs 400mn (Rs 630mn in Q4FY23).
- **API:** API business reported healthy 14% YoY growth on the back of improved demand for some products. Generally, non-beta-lactam antibiotics have a better gross margin than beta-lactam drugs.
- **ANDA approval and launch activity:** ARBP filed 12 abbreviated new drug applications (ANDA) including 1 injectable with the USFDA in Q1FY24 and received final approval for 19 ANDAs including 7 injectables during the same period. On the launch front, it introduced 15 products including 5 injectables during the quarter. Cumulatively, ANDA filing now stands at 814 (169 injectables), with 167 ANDAs (39 injectables) pending for approval.
- **R&D:** R&D spend stood at Rs 3.9bn in Q1FY24 or 5.7% of revenue vs. Rs 4.1bn in Q4FY23 or 6.3%.
- **New projects:** New projects in India and China are to be commercialised by Q1FY25. The penicillin-G PLI project is targeted to be completed by the end of FY24. For biosimilars, commercialisation is scheduled for FY25 onwards.
- **Capex:** Net capex for the quarter stood at ~US\$ 95.3mn, including an investment of ~US\$ 34mn in the Penicillin-G PLI project and ~US\$ 12mn for various new businesses and markets. Total PLI (Penicillin-G) capex up to 30 June 2023 was ~US\$ 160mn.
- **Investment in biosimilars:** Total spend in biosimilars (capital and revenue) up to 30 June stood at ~US\$ 280mn.
- **Cash position:** Free cash flow generation in Q1 before PLI investments and investment in new markets was US\$ 29.5mn. Net cash including investments as on 30 June was ~US\$ 178mn.
- **Debt and finance cost:** Gross debt stood at US\$ 644mn and average finance cost was 4.7%.
- **Regulatory update:** Of the 18 USFDA regulated units, 17 have voluntary action indicated (VAI) status while 1 is under a warning letter.

## Valuation methodology

Following the strong Q1FY24 print on the back of an improved business environment in the US and Europe and better margin guidance, we raise our FY24-FY25 EBITDA estimates by 11-12% and increase our FY25E EV/EBITDA multiple to 9x (from 7x) – in line with the five-year average. Our TP thus rises to Rs 880 (from Rs 635). Even so, we downgrade our rating from BUY to HOLD as the stock has rallied ~45% in the last three months and offers low upside potential at prevailing valuations of 10.2x/8.8x FY24E/ FY25E EV/EBITDA.

**Fig 7 – Revised estimates**

(Rs bn)	New		Old		Change (%)	
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
Sales	271.1	291.4	258.8	274.5	4.8	6.2
EBITDA	48.9	55.8	44.1	49.9	10.7	11.8
EBITDA margin (%)	18.0	19.1	17.1	18.2	96bps	96bps
EPS (Rs)	49.5	55.8	44.7	52.19	10.8	7.0

Source: BOBCAPS Research

**Fig 8 – Key assumptions**

Revenue (Rs bn)	FY23A	FY24E	FY25E
US	116.5	128.2	138.5
Europe	64.3	70.7	74.2
Emerging Markets	19.7	21.7	23.9
Antiretrovirals	9.5	8.6	9.2
API	38.5	41.9	45.7

Source: Company, BOBCAPS Research

## Key risks

Key upside risks to our estimates are:

- **gRevlimid launch:** The upcoming launch of gRevlimid in Oct'23 could take margins above expectations.
- **Improving US demand:** Further improvement in the US generic OSD/injectable landscape could push sales higher than our assumptions.

Key downside risks to our estimates are:

- **Price erosion in the US:** ARBP has been facing price erosion in the US market which is affecting margins, but now showing signs of stabilising. Any further increase in competitive intensity will ratchet up margin pressure.
- **US approval delays:** Delays in key approvals and execution hurdles are risk factors.
- **Regulatory risk:** ARBP supplies to the US from multiple plants. Its key facilities are Unit 3, Unit 7, Unit 10, Eugia and Unit 4. Any adverse action by the USFDA at these facilities can impact our earnings estimates.

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Ajanta Pharma	AJP IN	2.7	1,739	1,860	BUY
Alembic Pharma	ALPM IN	1.9	791	615	HOLD
Alkem Labs	ALKEM IN	5.5	3,795	3,300	SELL
Aurobindo Pharma	ARBP IN	6.2	872	880	HOLD
Cipla	CIPLA IN	12.1	1,236	1,250	BUY
Divi's Labs	DIVI IN	12.1	3,731	3,200	HOLD
Dr Reddy's Labs	DRRD IN	11.8	5,823	4,900	HOLD
Eris Lifesciences	ERIS IN	1.4	826	955	BUY
Glenmark Life Sciences	GLS IN	1.0	646	620	HOLD
Laurus Labs	LAURUS IN	2.5	385	340	HOLD
Lupin	LPC IN	6.0	1,082	800	SELL
Sun Pharma	SUNP IN	33.1	1,134	1,160	HOLD

Source: BOBCAPS Research, NSE | Price as of 14 Aug 2023

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
<b>Total revenue</b>	<b>2,47,749</b>	<b>2,34,555</b>	<b>2,48,554</b>	<b>2,71,092</b>	<b>2,91,396</b>
EBITDA	53,337	43,868	37,582	48,857	55,785
Depreciation	10,554	11,265	12,446	12,959	13,985
EBIT	42,783	32,603	25,136	35,899	41,800
Net interest inc./(exp.)	(745)	(486)	(1,405)	(530)	(983)
Other inc./(exp.)	2,773	2,504	3,254	3,340	2,796
Exceptional items	0	0	0	0	0
EBT	44,811	34,620	26,985	38,708	43,613
Income taxes	20,098	7,256	6,849	9,677	10,903
Extraordinary items	29,182	(580)	(744)	0	0
Min. int./Inc. from assoc.	543	302	118	0	0
<b>Reported net profit</b>	<b>53,351</b>	<b>26,482</b>	<b>19,275</b>	<b>29,031</b>	<b>32,710</b>
Adjustments	(29,182)	580	744	0	0
<b>Adjusted net profit</b>	<b>24,170</b>	<b>27,062</b>	<b>20,018</b>	<b>29,031</b>	<b>32,710</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
Accounts payables	27,947	27,031	38,713	37,136	39,917
Other current liabilities	29,831	30,400	31,178	32,531	34,968
Provisions	3,291	3,424	3,733	4,071	4,376
Debt funds	52,373	28,513	52,862	19,959	37,003
Other liabilities	0	0	0	0	0
Equity capital	586	586	586	586	586
Reserves & surplus	2,19,923	2,46,378	2,64,934	2,91,035	3,20,816
Shareholders' fund	2,20,509	2,46,964	2,65,520	2,91,621	3,21,401
<b>Total liab. and equities</b>	<b>3,33,950</b>	<b>3,36,331</b>	<b>3,92,005</b>	<b>3,85,318</b>	<b>4,37,666</b>
Cash and cash eq.	54,680	41,900	60,722	50,837	90,155
Accounts receivables	35,033	40,123	44,664	48,277	51,892
Inventories	90,266	75,539	85,112	92,840	99,793
Other current assets	23,711	26,006	31,943	21,958	23,603
Investments	5,910	9,972	5,428	5,428	5,428
Net fixed assets	68,866	77,284	79,954	81,795	82,611
CWIP	30,615	37,472	53,900	53,900	53,900
Intangible assets	24,870	28,036	30,283	30,283	30,283
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>3,33,950</b>	<b>3,36,331</b>	<b>3,92,005</b>	<b>3,85,318</b>	<b>4,37,666</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23A	FY24E	FY25E
<b>Cash flow from operations</b>	<b>55,282</b>	<b>45,361</b>	<b>25,842</b>	<b>41,278</b>	<b>40,987</b>
Capital expenditures	(5,977)	(22,049)	(27,123)	(14,800)	(14,800)
Change in investments	(363)	(4,061)	4,544	0	0
Other investing cash flows	0	0	0	0	0
<b>Cash flow from investing</b>	<b>(6,340)</b>	<b>(26,110)</b>	<b>(22,579)</b>	<b>(14,800)</b>	<b>(14,800)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(4,494)	(23,860)	24,349	(32,903)	17,045
Interest expenses	(745)	(486)	(1,405)	(530)	(983)
Dividends paid	(2,930)	(2,930)	(2,930)	(2,930)	(2,930)
Other financing cash flows	(14,515)	(4,755)	(4,457)	0	0
<b>Cash flow from financing</b>	<b>(22,684)</b>	<b>(32,031)</b>	<b>15,558</b>	<b>(36,363)</b>	<b>13,132</b>
<b>Chg in cash &amp; cash eq.</b>	<b>26,258</b>	<b>(12,780)</b>	<b>18,822</b>	<b>(9,885)</b>	<b>39,318</b>
<b>Closing cash &amp; cash eq.</b>	<b>54,680</b>	<b>41,900</b>	<b>60,722</b>	<b>50,837</b>	<b>90,155</b>

### Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23A	FY24E	FY25E
Reported EPS	91.1	45.2	32.9	49.5	55.8
Adjusted EPS	41.3	46.2	34.2	49.5	55.8
Dividend per share	2.5	2.5	2.5	2.5	2.5
Book value per share	376.8	422.0	453.7	498.3	549.2

### Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23A	FY24E	FY25E
EV/Sales	2.2	2.2	2.0	1.8	1.7
EV/EBITDA	10.3	11.9	13.4	10.2	8.8
Adjusted P/E	21.1	18.9	25.5	17.6	15.6
P/BV	2.3	2.1	1.9	1.7	1.6

### DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23A	FY24E	FY25E
Tax burden (Net profit/PBT)	53.9	78.2	74.2	75.0	75.0
Interest burden (PBT/EBIT)	104.7	106.2	107.4	107.8	104.3
EBIT margin (EBIT/Revenue)	17.3	13.9	10.1	13.2	14.3
Asset turnover (Rev./Avg TA)	24.8	21.4	20.9	21.5	21.7
Leverage (Avg TA/Avg Equity)	1.3	1.2	1.2	1.1	1.1
Adjusted ROAE	12.4	11.6	7.8	10.4	10.7

### Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23A	FY24E	FY25E
<b>YoY growth (%)</b>					
Revenue	7.3	(5.3)	6.0	9.1	7.5
EBITDA	10.5	(17.8)	(14.3)	30.0	14.2
Adjusted EPS	(15.8)	12.0	(26.0)	45.0	12.7
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	21.5	18.7	15.1	18.0	19.1
EBIT margin	17.3	13.9	10.1	13.2	14.3
Adjusted profit margin	9.8	11.5	8.1	10.7	11.2
Adjusted ROAE	12.4	11.6	7.8	10.4	10.7
ROCE	18.2	12.8	9.6	12.5	13.3
<b>Working capital days (days)</b>					
Receivables	52	62	66	65	65
Inventory	133	118	125	125	125
Payables	41	42	57	50	50
<b>Ratios (x)</b>					
Gross asset turnover	1.9	1.5	1.4	1.4	1.4
Current ratio	3.3	3.0	3.0	2.9	3.3
Net interest coverage ratio	57.4	67.0	17.9	67.7	42.5
Adjusted debt/equity	0.0	(0.1)	0.0	(0.1)	(0.2)

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

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

**BUY** – Expected return >+15%

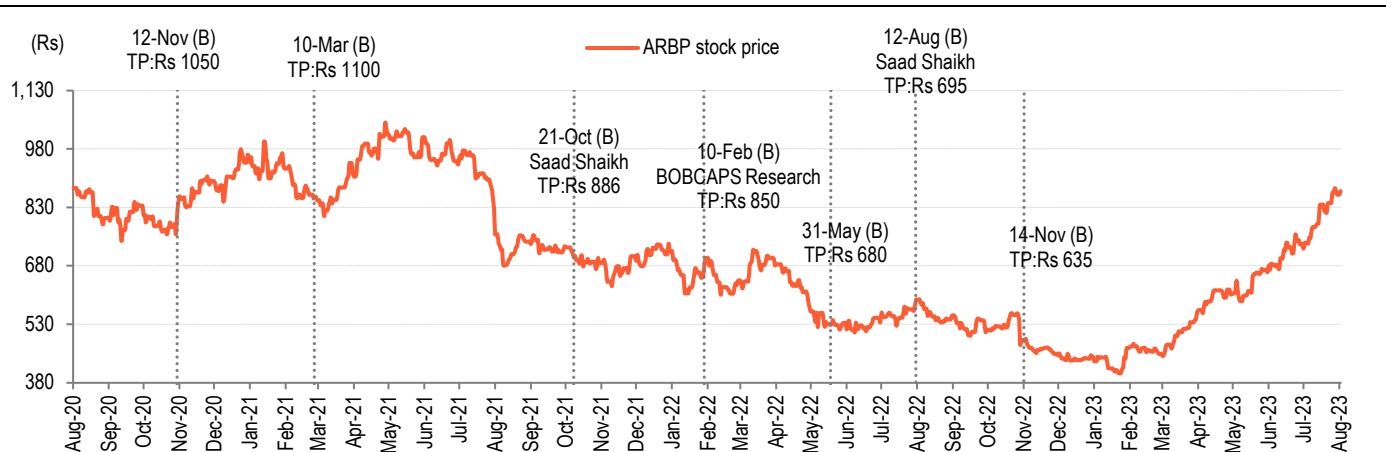
**HOLD** – Expected return from -6% to +15%

**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): AUROBINDO PHARMA (ARBP IN)



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

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