

RESEARCH

BOB Economics Research | RBI policy

Inflation underestimated, growth still a priority

Aurobindo Pharma | Target: Rs 850 | +24% | BUY

Headwinds continue; Plans India formulations foray

Alembic Pharma | Target: Rs 905 | +19% | BUY

US business weak but showing signs of stabilising

SUMMARY

India Economics: RBI policy

RBI has kept all policy rates unchanged. There has been focus on liquidity management. We believe the 4.5% inflation forecast for FY23, is on the lower side in the wake of crude running at US\$ +90/bbl and high global commodity prices among others. Our forecast for CPI is ~5.5% in FY22 and at 5.0-5.5% in FY23. Growth forecast of RBI at 7.8% seems realistic. We expect RBI to remain on hold in the coming two policies as well.

[Click here for the full report.](#)

Aurobindo Pharma

- Q3 revenue declined 6% YoY despite 48% growth in APIs as US (-13%) and ARV (-65%) business contracted
- US price erosion and high input & freight costs depleted gross/EBITDA margin by 530bps/460bps YoY
- We cut FY22/FY23 EBITDA by 16%/5% and reset our EV/EBITDA multiple to 7.5x (vs. 8.5x); on rollover, we have a TP of Rs 850 (vs. Rs 886) – BUY

[Click here for the full report.](#)

Daily macro indicators

Indicator	08-Feb	09-Feb	Chg (%)
US 10Y yield (%)	1.96	1.94	(2)
India 10Y yield (%)	6.81	6.81	0
USD/INR	74.75	74.81	(0.1)
Brent Crude (US\$/bbl)	90.8	91.6	0.8
Dow	35,463	35,768	0.9
Hang Seng	24,329	24,830	2.1
Sensex	57,809	58,466	1.1
India FII (US\$ mn)	07-Feb	08-Feb	Chg (\$ mn)
FII-D	20.2	(58.7)	(78.8)
FII-E	130.1	9.3	(120.8)

Source: Bank of Baroda Economics Research

BOBCAPS Research

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Alembic Pharma

- Q3 revenue dipped 3% YoY on a steep decline in US (-23%) and API (-8%) business, despite growth in India (+17%) and ROW (+13%)
- US revenue grew QoQ to US\$ 53mn but plunged YoY due to the absence of one-offs. Higher freight and RM cost weighed on margins
- We cut FY22-FY24 EBITDA by 4-10% and roll over to a new TP of Rs 905 (vs. Rs 980) based on 11x FY24E EV/EBITDA (vs. 13x); retain BUY

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RBI POLICY

10 February 2022

Inflation underestimated, growth still a priority

RBI has kept all policy rates unchanged. There has been focus on liquidity management. We believe the 4.5% inflation forecast for FY23, is on the lower side in the wake of crude running at US\$ +90/bbl and high global commodity prices among others. Our forecast for CPI is ~5.5% in FY22 and at 5.0-5.5% in FY23. Growth forecast of RBI at 7.8% seems realistic. We expect RBI to remain on hold in the coming two policies as well.

Dipanwita Mazumdar
Economist

RBI maintained status quo: As against our expectation of a 25bps hike in reverse repo rate, RBI kept policy rates unchanged. Its forecast for FY22 is unchanged at 5.3%. There has been no mention of liquidity withdrawal and focus is on management through the use of VRR and VRRR. Stance has also been kept accommodative with the indication that it will remain so in next year too.

CPI forecast at 5.3% for FY22 and 4.5% at FY23: RBI has kept inflation forecast for FY22 unchanged at 5.3%, with Q4FY22 print expected at 5.7%, as said in the Dec'21 policy. Here few things need to be mentioned. 1) During Dec'21 policy, crude was trading at ~US\$ 70/bbl, 2) global inflation was less of an issue and 3) global central banks were not so hawkish. But things have changed with crude reigning at ~US 92/bbl, geopolitical tensions increasing and elevated supply concerns with core inflation remaining fairly sticky. We believe the full pass through of input cost inflation is still to be realized. We expect transport and communication inflation to increase post State elections. Thus, the trajectory of inflation as projected by RBI (between 4- 5% in FY23), is on the lower side. Notably, the FY23 CPI projections are also 20bps lower compared to that in Apr'21 policy when crude was at \$ 60/bbl.

Where inflation will go: We believe based on the underlying situation of elevated supply cost in terms of escalated energy cost and lengthened supply delivery timelines, CPI is likely to be elevated. We expect it to settle at ~5.5% in FY22 and at 5.0-5.5% in FY23, with risks tilted to the upside. Notably, another upside risk to inflation is the possibility of a below normal monsoon. Statistically, with six successive monsoons, there could be a sub-optimal one this year. Thus it might push food inflation further in the coming fiscal. Our forecast also incorporates 10% increase in crude price which will impact CPI by ~0.4-0.6%.

Growth forecast realistic: RBI has estimated growth to be at 7.8% in FY23. This is in line with our estimation of 7.75-8% in FY23. RBI has pointed that better rabi sowing, pick up in exports, capex of government and rising business investment which will make up for slower growth in consumption.



BUY

TP: Rs 850 | ▲ 24%

AUROBINDO PHARMA

Pharmaceuticals

10 February 2022

Headwinds continue; Plans India formulations foray

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- US price erosion and high input & freight costs depleted gross/EBITDA margin by 530bps/460bps YoY
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Surajit Pal | Saad Shaikh
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API sales recover; US and ARV businesses decline: ARBP reported a 6% YoY decline in Q3FY22 revenue primarily on account of a 13% drop in US business and a continued slowdown in ARVs (-65%). APIs reported a strong recovery with 48% YoY growth, benefitting from improved demand for key products.

US continues to see pricing pressure: US generics sales declined by 8% CC QoQ (ex-Natrol) to US\$ 369mn in Q3 vs. US\$ 400mn in Q2 due to heavy price erosion and high inventory with channel partners. With stronger competitive intensity all through FY22, ARBP has witnessed 9% YoY price erosion and shelf stock adjustment of US\$ 11mn in Q3 and US\$ 45mn in 9MFY22, while benefitting from only a miniscule penalty for non-supply during the contract period.

High input and freight costs weigh on margins: ARBP witnessed sharp gross margin contraction of 530bps YoY (-355bps QoQ) to 54.3% due to continued US price erosion and high input & freight costs, which shaved 460bps YoY (-300bps QoQ) off the EBITDA margin. Higher raw material costs and pricing headwinds had a negative impact of 150bps on gross margin, with a 125bps hit from an unfavourable product mix (strong API sales). RM and freight costs increased 8-10% YoY.

Domestic branded formulations foray: Given strong cash flow generation, ARBP has announced that it is actively evaluating an entry into the India formulations business through a combination of acquisitions and organic launches. The company plans to reach revenues of Rs 10bn in three years from the date of first launch. As per management, more clarity will emerge by Q1FY23.

Maintain BUY: The stock trades at attractive valuations of 6.9x/5.8x FY23E/ FY24E EV/EBITDA. We cut our FY22/FY23 EBITDA estimates by 15%/5% to factor in the Q3 performance – retain BUY with a revised TP of Rs 850 (Rs 886 earlier) as we roll valuations forward to FY24 and move to a lower 7.5x EV/EBITDA multiple (8.5x earlier), implying a P/E of 12x. Our target multiple reflects a continued 45% discount to other frontline stocks (SUNP, CIPLA, DRRD) due to ARBP's low branded sales and high US exposure.

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	ARBP IN/Rs 684
Market cap	US\$ 5.4bn
Free float	48%
3M ADV	US\$ 19.1mn
52wk high/low	Rs 1,064/Rs 590
Promoter/FPI/DII	52%/22%/16%

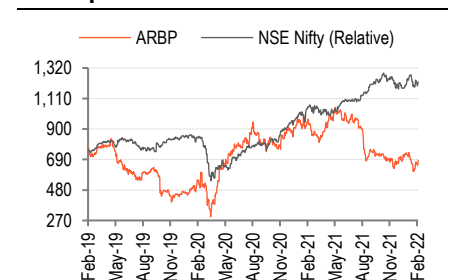
Source: NSE | Price as of 10 Feb 2022

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	2,47,746	2,38,108	2,64,197
EBITDA (Rs mn)	53,334	45,792	55,779
Adj. net profit (Rs mn)	25,203	27,825	34,726
Adj. EPS (Rs)	43.0	47.5	59.3
Consensus EPS (Rs)	43.0	52.0	59.2
Adj. ROAE (%)	12.9	11.9	13.3
Adj. P/E (x)	15.9	14.4	11.5
EV/EBITDA (x)	8.3	9.0	6.9
Adj. EPS growth (%)	(12.2)	10.4	24.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



BUY
 TP: Rs 905 | ▲ 19%

ALEMBIC PHARMA

Pharmaceuticals

11 February 2022

US business weak but showing signs of stabilising

- Q3 revenue dipped 3% YoY on a steep decline in US (-23%) and API (-8%) business, despite growth in India (+17%) and ROW (+13%)
- US revenue grew QoQ to US\$ 53mn but plunged YoY due to the absence of one-offs. Higher freight and RM cost weighed on margins
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Strong growth in India and ROW muted by drop in US and API sales: US business dropped 23% YoY in Q3FY22, prompting a 3% YoY revenue decline for ALPM despite strong India (+17%) and ROW growth (+13%) off a high base. API business declined 8% YoY during the quarter due to an unfavourable base.

US business showing signs of stabilising: US revenue rose 13% QoQ to US\$ 53mn, indicating signs of stability in the business which saw a sharp YoY contraction due to the absence of one-off opportunities and increased competition that led to price erosion in a few large products.

New launches to combat price erosion: ALPM plans to launch some complex products in the US market over the next six months, including one inhalation product (Formoterol Fumarate) and complex oral solid dosages on the first-day launch of generics. During the quarter, the company launched six products and plans to introduce an additional five in Q4FY22. Management expects new products to compensate for the revenue loss in its existing US portfolio due to price erosion.

Near-term EBITDA margin guided at 20-21%: ALPM's gross/EBITDA margin contracted 465bps/770bps YoY to 73.1%/20.1% in Q3 on account of higher raw material and freight cost coupled with supply chain disruptions. Management expects freight charges to remain elevated in Q4. With a focus on cost rationalisation, new launches and market share gains in existing products, ALPM expects to maintain a 20-21% EBITDA margin in the near term.

Maintain BUY: The stock is currently trading at 12.1x/9.2x FY23E/FY24E EV/EBITDA (18.8x/14.4x P/E). We cut our FY22-FY24 EBITDA estimates by 4-10% to factor in margin pressures amid pricing issues in the US and rising costs. On rollover to FY24 valuations, we arrive at a revised TP of Rs 905 (Rs 980) set at a reduced EV/EBITDA multiple of 11x (implied P/E of 17x) vs. 13x earlier. Our target multiple is at 35% discount to peers such as ALKEM and AJP. Given the attractive valuations, we retain our BUY rating on the stock.

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	ALPM IN/Rs 758
Market cap	US\$ 2.0bn
Free float	31%
3M ADV	US\$ 4.2mn
52wk high/low	Rs 1,038/Rs 714
Promoter/FPI/DII	69%/6%/11%

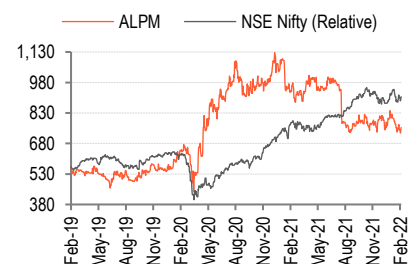
Source: NSE | Price as of 10 Feb 2022

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	53,940	51,566	55,581
EBITDA (Rs mn)	15,584	10,163	12,323
Adj. net profit (Rs mn)	11,473	6,609	7,926
Adj. EPS (Rs)	60.0	33.6	40.3
Consensus EPS (Rs)	60.0	34.5	39.8
Adj. ROAE (%)	28.5	12.4	13.5
Adj. P/E (x)	12.6	22.6	18.8
EV/EBITDA (x)	10.4	15.5	12.1
Adj. EPS growth (%)	35.1	(43.9)	19.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



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.

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