

BUY

TP: Rs 480 | ▲ 34%

LAURUS LABS

Pharmaceuticals

29 January 2021

Solid margins despite higher API mix – TP raised to Rs 480

Laurus Labs reported another solid beat in Q3FY21 fuelled by strong growth in the API and synthesis segments. Revenue and EBITDA beat estimates by 14% each. EBITDA grew 188% YoY (14% QoQ) with margins at 33%, aided by a better mix and operating leverage. Formulation (FDF) sales grew 47% YoY, ARVs 50% QoQ, oncology API 37% YoY, and synthesis 62% YoY. Laurus expects to sustain Q3 margins and has retained FY21-FY22 capex at Rs 12bn on order visibility. We raise FY21-FY23 EPS 8-10% and roll to a new Mar'22 TP of Rs 480 (vs. Rs 410).

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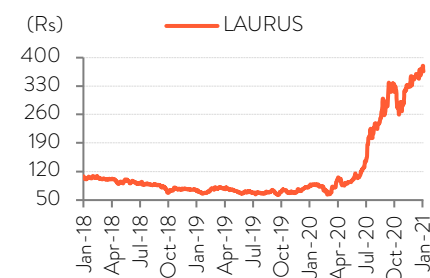
Solid execution: With execution gaining momentum, we raise FY21-FY23 EPS estimates by ~10%. ARV API sales delivered a strong beat led by higher volumes in first-line products (EFA & DTG) and stable pricing. The Q3 API base is sustainable, per management. Synthesis sales reported a 20% beat (+62% YoY, +10% QoQ), led by uptake in commercial supplies for four products. The order book across high-margin segments of formulations, synthesis (non-Aspen CDMO) and APIs is intact. Laurus expects phase-1 of brownfield expansion to start from Aug'21 and has added several new customers under CMO programs.

Ticker/Price	LAURUS IN/Rs 358
Market cap	US\$ 2.6bn
Shares o/s	535mn
3M ADV	US\$ 18.5mn
52wk high/low	Rs 386/Rs 59
Promoter/FPI/DII	29%/24%/3%

Source: NSE

Margins hold strong despite high ARV API mix: Q3 and 9MFY21 gross margins were strong at 55% each. EBITDA margins came in at 33% and 31.5% respectively despite higher ARV API contribution (44% of sales in Q3 vs. 33% in Q2), reflecting improvement in pricing and volumes. Per Laurus, 9M margins should sustain over the next two years. Strong margins were underpinned by a favourable FDF/synthesis mix and operating leverage across segments.

STOCK PERFORMANCE



Source: NSE

Earnings call highlights: (1) ARV FDF sustaining strong multi-month dispensing trend. (2) Capex of Rs 4.3bn incurred in 9M (incl. CWIP). (3) Laurus has highest market share in DTG APIs and third highest in formulations; not worried about competition. (4) Commenced marketing of in-licensed products in the US.

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	22,919	28,317	45,300	51,103	58,292
EBITDA (Rs mn)	3,560	5,645	14,442	16,463	19,071
Adj. net profit (Rs mn)	937	2,553	9,270	10,864	12,892
Adj. EPS (Rs)	1.8	4.8	17.3	20.3	24.1
Adj. EPS growth (%)	(36.8)	172.3	263.2	17.2	18.7
Adj. ROAE (%)	6.2	15.3	42.5	35.2	30.9
Adj. P/E (x)	204.3	75.0	20.7	17.6	14.9
EV/EBITDA (x)	56.5	35.8	14.0	12.4	10.6

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	Q3FY21E	Var. (%)	9MFY21	9MFY20	YoY (%)
Net Sales	12,884	7,295	76.6	11,388	13.1	11,344	13.6	34,015	19,925	23.6
EBITDA	4,263	1,483	187.6	3,739	14.0	3,744	13.9	10,787	3,695	57.6
Depreciation	516	476	-	510	-	510	-	1,514	1,412	-
EBIT	3,747	1,007	-	3,229	-	3,234	-	9,273	2,283	-
Interest	174	208	-	137	-	137	-	462	689	-
Other Income	69	19	-	51	-	51	-	191	78	-
PBT	3,642	818	345.2	3,143	15.9	3,148	15.7	9,002	1,671	145.1
Less: Taxation	913	82	-	720	-	692	-	2,130	217	-
Less: Minority Interest	0	0	-	0	-	0	-	0	0	-
Recurring PAT	2,729	736	270.9	2,423	12.6	2,455	11.1	6,872	1,454	172.2
Exceptional items	0	0	-	0	-	0	-	-	-	-
Reported PAT	2,729	736	270.9	2,423	12.6	2,455	11.1	6,872	1,454	172.2
Key Ratios (%)										
Gross Margin	54.7	50.6	416	56.0	(124)	54.5	-	55.0	50.1	-
EBITDA Margin	33.1	20.3	1276	32.8	25	33.0	-	31.7	18.5	-
Tax / PBT	25.1	10.1	-	22.9	-	22.0	-	23.7	13.0	-
NPM	21.2	10.1	-	21.3	-	21.6	-	20.2	7.3	-
EPS (Rs)	5.1	1.4	-	4.5	-	4.6	-	12.8	2.7	-

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	Q3FY21E	Var. (%)	9MFY21	9MFY20	YoY (%)
Generics – API	7,310	3,592	103.5	5,710	28.0	5,542	31.9	18,240	11,524	(13.0)
ARVs	5,680	2,135	166.0	3,790	49.9	3,700	53.5	12,830	7,684	(26.0)
Oncology	640	468	36.8	860	(25.6)	655	(2.3)	2,010	1,515	(3.1)
Other API	990	989	0.1	1,060	(6.6)	1,187	(16.6)	3,400	2,325	71.8
Synthesis	1,270	782	62.4	1,160	9.5	1,056	20.3	3,430	2,371	51.0
Formulations	4,300	2,921	47.2	4,520	(4.9)	4,746	(9.4)	12,340	5,580	1403.6
Net Sales	12,880	7,295	76.6	11,390	13.1	11,344	13.5	34,010	19,475	31.6

Source: Company, BOBCAPS Research

Valuation methodology

We retain our BUY rating on Laurus following a consistent increase in EBITDA share from high-margin businesses (synthesis, formulations, other APIs ex-ARV) and sharp turnaround in return ratios (visible in the 9M beat), which could spur a stock rerating in coming years. Over the next two years, these high-margin segments – supported by recalibration in the procurement strategies of global companies – are expected to drive >90% of incremental EBITDA and aid sustained ROIC of >35% from ~14% in FY20.

Given the solid order book and ahead-of-schedule execution, Laurus has increased its total capex to Rs 12bn (from Rs 7bn) for FY21 and FY22 combined. This should be viewed positively as incremental capex would not be FCF-dilutive, in our view.

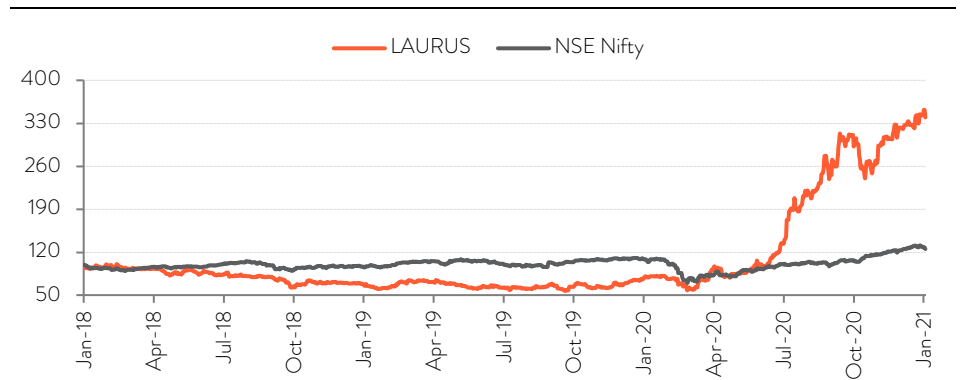
The share price has rallied sharply, more than tripling from Mar'20 lows, but current valuations of 10x FY23E EBITDA are still below the three-year historical mean of 12x one-year forward. We increase our FY21-FY23 EBITDA forecasts by 6-7% to factor in the solid 9MFY21 beat, higher gross margins and sustainable rise in operating leverage. Our Mar'22 target price rises to Rs 480 (from Rs 410) as we roll valuations over, ascribing an unchanged one-year forward EV/EBITDA multiple of 14x to the stock. Maintain BUY.

FIG 3 – REVISED ESTIMATES

(Rs bn)	New			Old			Change (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Sales	45.3	51.1	58.3	43.4	49.8	57.0	4.4	2.7	2.3
EBITDA	14.4	16.5	19.1	13.5	15.5	18.1	7.1	6.1	5.6
EBITDA margin (%)	31.9	32.2	32.7	31.1	31.2	31.7	81bps	102bps	101bps
EPS (Rs)	17	20	24	16	19	22	8.9	7.8	7.5

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **Higher concentration and pricing pressure in ARVs:** The ARV segment accounted for 36% of revenues in FY20 (from 61% in FY19) and has witnessed pricing pressure in the past two years. A shift in the treatment regime from Efavirenz to Dolutegravir has adversely impacted gross margins. To arrest the margin compression and business decline in ARVs, management has taken steps toward (1) backward integration of some APIs including FTC and Lamivudine, and (2) rapid expansion of the non-ARV business. This, in our view, should mitigate the profitability risk.
- **Regulatory risks:** Units 1 and 3 are critical as they account for 80% of the topline (mainly catering to the API and synthesis businesses). Unit 2 is Laurus' sole US formulations facility. All three units have recently received establishment inspection reports (EIR).
- **Delay in formulation business ramp-up:** Any delays in product approval can adversely affect the planned scale-up and our FY21 forecast for the formulations business.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	22,919	28,317	45,300	51,103	58,292
EBITDA	3,560	5,645	14,442	16,463	19,071
Depreciation	1,642	1,873	2,034	2,095	2,445
EBIT	1,918	3,773	12,408	14,368	16,626
Net interest income/(expenses)	(882)	(896)	(687)	(774)	(704)
Other income/(expenses)	161	59	13	158	607
Exceptional items	0	0	0	0	0
EBT	1,197	2,936	11,735	13,752	16,528
Income taxes	260	383	2,464	2,888	3,636
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	937	2,553	9,270	10,864	12,892
Adjustments	0	0	0	0	0
Adjusted net profit	937	2,553	9,270	10,864	12,892

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	4,882	6,156	8,688	9,801	11,179
Other current liabilities	1,411	1,625	3,171	3,577	4,080
Provisions	365	568	908	1,025	1,169
Debt funds	11,068	11,456	13,518	12,289	11,172
Other liabilities	0	0	0	0	0
Equity capital	1,064	1,069	1,069	1,069	1,069
Reserves & surplus	14,516	16,623	24,891	34,753	46,643
Shareholders' fund	15,581	17,692	25,960	35,822	47,712
Total liabilities and equities	33,307	37,497	52,246	62,514	75,313
Cash and cash eq.	30	17	185	2,903	9,160
Accounts receivables	7,099	7,914	12,163	13,301	15,172
Inventories	6,819	9,052	13,652	16,521	18,845
Other current assets	1,939	2,545	4,983	5,621	6,412
Investments	34	34	34	34	34
Net fixed assets	16,072	17,068	19,034	21,939	24,494
CWIP	1,096	672	2,000	2,000	1,000
Intangible assets	218	195	195	195	195
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	33,307	37,497	52,246	62,514	75,313

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	2,579	4,425	11,305	12,959	15,337
Interest expenses	0	0	0	0	0
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(402)	(1,963)	(6,869)	(3,010)	(2,960)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	2,177	2,462	4,436	9,949	12,377
Capital expenditures	(3,117)	(2,374)	(4,000)	(5,000)	(5,000)
Change in investments	0	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(3,117)	(2,374)	(4,000)	(5,000)	(5,000)
Equities issued/Others	4	5	0	0	0
Debt raised/repaid	591	388	2,062	(1,229)	(1,117)
Interest expenses	0	0	0	0	0
Dividends paid	(176)	0	(1,002)	(1,002)	(1,002)
Other financing cash flows	519	(493)	(1,328)	0	1,000
Cash flow from financing	939	(100)	(268)	(2,231)	(1,120)
Changes in cash and cash eq.	(1)	(13)	168	2,718	6,258
Closing cash and cash eq.	29	17	185	2,903	9,160

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	1.8	4.8	17.3	20.3	24.1
Adjusted EPS	1.8	4.8	17.3	20.3	24.1
Dividend per share	1.5	1.5	1.5	1.5	1.5
Book value per share	29.1	33.1	48.6	67.0	89.3

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	8.8	7.1	4.5	4.0	3.5
EV/EBITDA	56.5	35.8	14.0	12.4	10.6
Adjusted P/E	204.3	75.0	20.7	17.6	14.9
P/BV	12.3	10.8	7.4	5.3	4.0

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	78.3	86.9	79.0	79.0	78.0
Interest burden (PBT/EBIT)	62.4	77.8	94.6	95.7	99.4
EBIT margin (EBIT/Revenue)	8.4	13.3	27.4	28.1	28.5
Asset turnover (Revenue/Avg TA)	22.1	25.4	33.0	29.2	27.2
Leverage (Avg TA/Avg Equity)	1.7	1.7	1.6	1.4	1.3
Adjusted ROAE	6.2	15.3	42.5	35.2	30.9

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	11.5	23.6	60.0	12.8	14.1
EBITDA	(13.9)	58.6	155.8	14.0	15.8
Adjusted EPS	(36.8)	172.3	263.2	17.2	18.7
Profitability & Return ratios (%)					
EBITDA margin	15.5	19.9	31.9	32.2	32.7
EBIT margin	8.4	13.3	27.4	28.1	28.5
Adjusted profit margin	4.1	9.0	20.5	21.3	22.1
Adjusted ROAE	6.2	15.3	42.5	35.2	30.9
ROCE	8.0	13.7	36.2	33.2	32.2
Working capital days (days)					
Receivables	113	102	98	95	95
Inventory	109	117	110	118	118
Payables	78	79	70	70	70
Ratios (x)					
Gross asset turnover	1.1	1.2	1.7	1.6	1.6
Current ratio	2.4	2.3	2.4	2.7	3.0
Net interest coverage ratio	2.2	4.2	18.1	18.6	23.6
Adjusted debt/equity	0.7	0.6	0.5	0.3	0.0

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

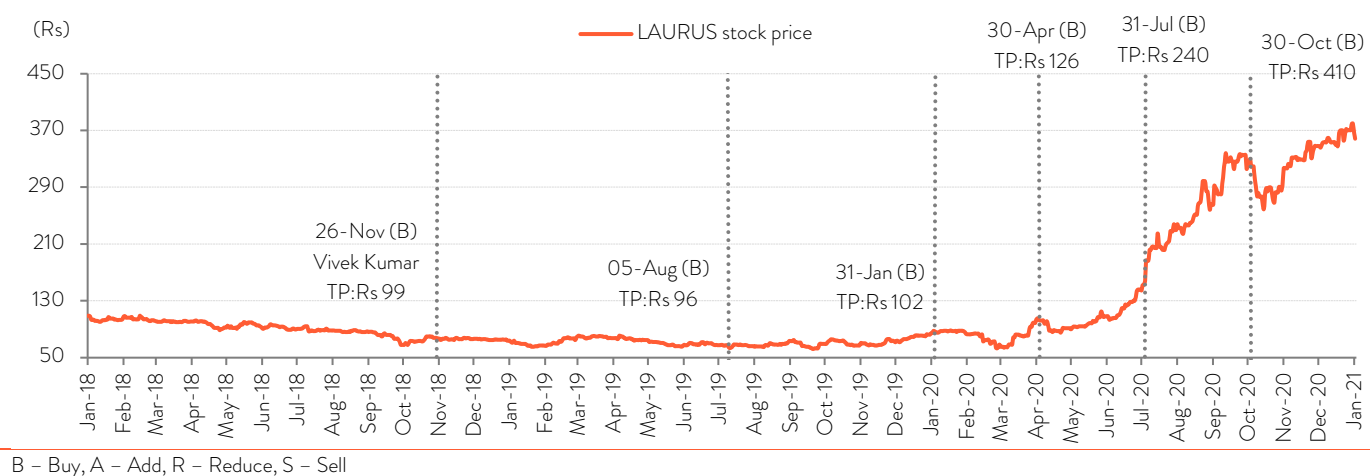
ADD – Expected return from >+5% to +15%

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)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): LAURUS LABS (LAURUS IN)



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