

5th May 2020

Alkem Laboratories–BUY

CMP : Rs.2,699
Target Price : Rs.3,278.0
Upside : 21%+
Stop Loss : Rs.2,390.0 (Closing basis)

Investment Thesis

Alkem Laboratories' 53% of total business depends upon domestic acute segment of which 50% is contributed by anti-infective (AI) segment. AI segment has grown at 5.2% CAGR over FY15-19 while Indian Pharmaceutical Market (IPM) grew at 10.8% CAGR during this period. The growth was impacted in the past three years due to macro events and poor season. However, FY20E is proving to be a blockbuster year for AI therapies due to strong season. It is witnessed that infectious diseases (respiratory/gastric/STDs) are still prevalent in India, hence, AI segment would continue to grow at IPM rate of ~10% YoY going forward. We expect, Alkem Laboratories can benefit in this segment by banking on its brand equity, strong field force and strong relationships with doctors. In the Chronic therapies, the company is seeing rapid growth and expects revenue double over next 4-5 years.

Alkem Laboratories has been a late entrant in the US market, however, it has not proved to be detrimental as it has grown its business by 1.8x during FY16-FY19. With large facilities are keeping satisfactory compliance and ~50% ANDAs still awaiting approval, Alkem Laboratories has significant headroom for growth over next 2-3 years. Alkem Laboratories is also engaged in several Para-IV litigations showing management's appetite for growing US business. Its St. Louis plant is under Official Action Indicated (OAI), but its contribution is <1% in the total business hence we expect no major impact on the entire business. We expect Alkem Laboratories' US business to grow at ~20% CAGR over FY19-22E with stable ~10% EBITDA margins.

Financials

- During the past 5 years, revenue of Alkem Laboratories grew at CAGR of 18.7% while PAT grew at CAGR of 11.8% in the same period.

Consol. (Rs.Mn.)	FY17	FY18	FY19	FY20E	FY21E
Revenue	56,875	63,918	73,572	84,608	97,299
EBITDA	9,990	10,089	11,148	12,820	14,743
% growth	17.1	1.0	10.5	15.0	15.0
PAT	8,920	6,309	7,605	9,210	10,591
EPS (INR)	74.6	52.8	63.6	77.0	88.6
P/E (x)	36.6	51.8	43.0	35.5	30.9
RoE (%)	20.0%	13.0%	14.0%	15.4%	16.1%

- Alkem Laboratories has reported 13.3% YoY growth in revenue to Rs.21,818mn in Q3FY20 due to better than estimated India sales growth of ~15% YoY led by 21% YoY growth of chronic therapy.

Stock Data

Market Cap (Rs. Mn)	3,27,728
Market Cap (\$ Mn)	4,286.8
Shares O/S (in Mn)	119.6
Avg. Volume (3 month)	145,000
52-Week Range (Rs.)	2,879.00/ 1,660.00

Shareholding Pattern

Promoters	66.04%
FIIIs	2.71%
Institutions	12.01%
Others (incl. body corporate)	19.24%

Performance (%)	1M	6M	1Yr
Absolute	23.4%	38.9%	58.8%
BSE Healthcare	44.0%	23.2%	0.6%

Key Ratios

Div Yield	0.6%
TTM PE	29.6x
ROE	16.0%
TTM EPS (Rs.)	92.5/-

- Alkem Laboratories' EBITDA grew by 45.4% YoY in Q3FY20 to Rs.4,533mn mainly due to better revenue growth and cost control initiative taken by the company in the recent past. As a result, EBITDA margin also grew by ~460bps YoY to 20.8% in Q3FY20.
- Alkem Laboratories' PAT grew significantly by 88.7% YoY to Rs.3,822mn due to better operating performance and lower tax outgo in the quarter.

Key Business Highlights

- Alkem Laboratories is ranked among top 5 players in the acute therapy segment, which constitutes over 80% of its overall domestic revenue. Anti-infectives, gastrointestinal, vitamins/minerals/nutrients and pain/analgesic are some of its major leading sub-segment.
- Alkem Laboratories has a fairly diverse portfolio of products includes brands like Clavam, Pan, Pan-D and Taxim-O, which feature amongst top 50 pharmaceutical brands in India.
- Alkem Laboratories 21 manufacturing facilities at multiple locations in India and the USA. It has cumulatively filed more than 125 ANDAs with the US FDA. Alkem Laboratories markets and sells products in the USA under its wholly owned subsidiary, Ascend.

Valuation

- Alkem Laboratories has a comprehensive portfolio of over 800 brands covering all the major therapeutic segments and a robust pan-India sales and distribution network. It has a strong and extensive pan-India distribution network of 11 warehouses, 40+ sales depots, 7000+ Stockists and 9,000 people in the field force covering all states including rural India. Apart from having a strong foothold in the domestic market, Alkem Laboratories also has presence in more than 50 international markets, with the United States being the key focus international market. Alkem Laboratories has 21 manufacturing facilities, with 19 being in India and 2 located in the USA. The major five locations involved in the sales operations overseas are USA, Australia, Chile, United Kingdom and Germany.
- Over the period, Alkem Laboratories has developed its mega brands like Pan, Pan-D and Ondem, which are the market leaders in their respective molecule in the gastro-intestinal segment. Gastro is going to be the key focus area for Alkem Laboratories within the acute therapy since there is a lot of untapped potential in its sub-segments.
- Alkem Laboratories features among the top 5 companies in Vitamins / Minerals and Nutrients. With changing lifestyles and increasing evidences of vitamin, mineral deficiency being common in India combined with new launches, we expect this segment to grow at ~10% CAGR in the years to come.
- With major focus on domestic acute segment, despite late entrant US business grew by 1.8x during FY16-FY19, comprehensive portfolio of over 800 brands, strong and extensive pan-India distribution network and developed its mega brands as market leaders, we value Alkem Laboratories at 37.0x FY21E EPS of Rs.88.60 to arrive at target price of Rs.3,278.00, an upside of 21%.

Risk & Concern

- Government guideline to change the mechanism of calculating the ceiling price of the drugs may impact the pricing and profitability of India business for Alkem Laboratories negatively as 20% of its product portfolio is under the coverage of Drug Price Control Orders (DPCO).
- Any negative observation by USFDA on any manufacturing facilities of Alkem Laboratories may affect the operations of the company.
- Government initiatives like Jan Aushadhi and traction in unbranded generics may adversely impact growth of Alkem Laboratories.

Graphs & Charts

Figure 1: Net Sales Trend

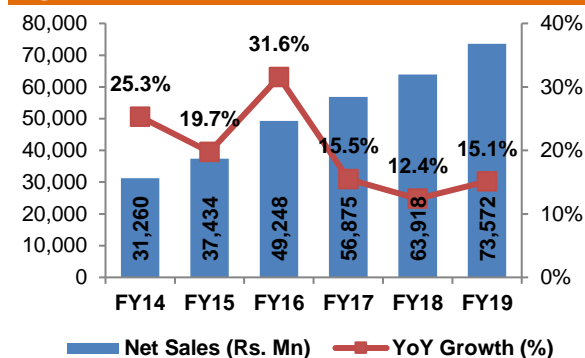


Figure 2: EBITDA & EBITDA Margin Trend

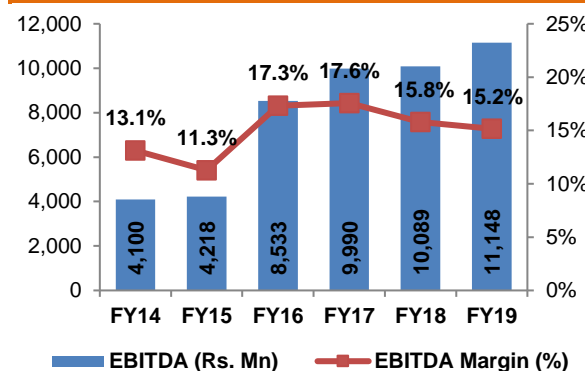


Figure 3: PAT Trend

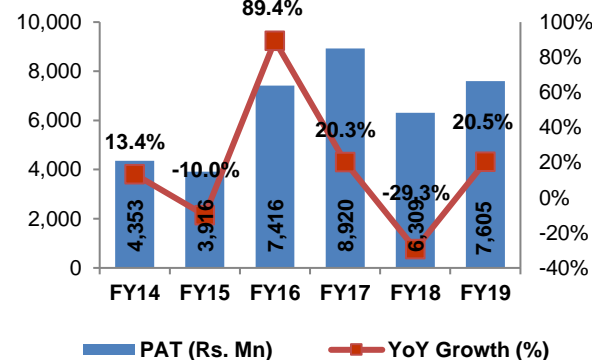
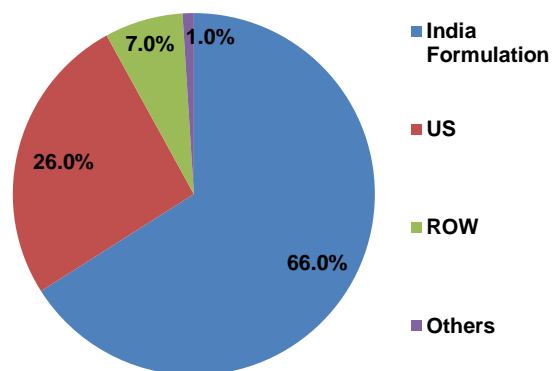


Figure 4: Region-wise Business Mix (FY19)



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