In-line results; Domestic business recovered strongly

Motilal Oswal

25 October 2016

Q2FY17 Results Update | Sector: Healthcare

Alembic Pharmaceuticals

TP: INR640 (-5%) **CMP: INR673** Neutral

BSE SENSEX S&P CNX 28,091 8.691 Bloomberg ALPM IN

Free float (%)	25.7
	,
Avg Val. (INR m)	93
1, 6, 12 Rel.Per (%)	1/1/-5
52-Week Range (INR)	727/514
M.Cap. (INR b) / (USD b)	127/1.9
Equity Shares (m)	188.5

Y/E MAR	2016 2	2018E	
Sales	31.5	31.9	38.5
EBITDA	10.0	6.7	8.9
NP	4.8	4.7	6.0
EPS (INR)	38.2	24.7	31.9
EPS Gro. (%)	154.6	-35.2	29.2
BV/Sh. (INR)	84.9	103.6	129.6
RoE (%)	38.8	26.2	27.4
RoCE (%)	50.6	24.6	26.2
P/E (x)	17.6	27.2	21.1
P/BV (x)	7.9	6.5	5.2
EV/EBITDA (x)	12.3	18.6	14.1
Estimate change		•	

TP change

Rating change

Alembic Pharma's (ALPM) 2Q results were broadly in line with our estimates.
Sales grew grew 19.4% QoQ to INR8.79b in 2Q (~11% above est) due to strong
grouth in India branded business and the US. However EDITOA margins

growth in India branded business and the US. However EBITDA margins contracted ~100bp sequentially and stood at 20.2% in 2Q, weighed down by higher R&D expense (up 160bps QoQ). PAT stood at INR1.2b, up 16% QoQ (inline with estimate).

Domestic and US business delivered strong growth: Domestic branded business delivered 19%QoQ growth whereas generic business remained flat sequentially. Strong branded business growth was explained by 22% YoY growth in acute segment (on the back of lower base and strong seasonality impact) and 16% YoY growth in specialty segment. International business grew ~14% QoQ on the back of ~23% growth in US business (~INR2.7b). Increase in US sales is primarily attributed to increase in market share of Abilify. We expect Abilify sales to come down as two new competitors have entered the market.

Concall takeaways: (a) Capex for FY17 to be ~INR6b (~INR10b over next 2 years); (b) ALPM launched 23 products through own frontend in the last 12 months; (c) R&D to be ~INR4-4.5b in FY17; (d) Oncology oral solids and injectable facilities to be operational by FY17 end; (e) Onco injectable filling will start from 2HFY18; (f) General injectable and Derma filings in US will start from FY19; (g) 12-16 ANDA approvals expected till FY18 end; (h) ~33 pending ANDAs, of which ~40% are Para IV/ FTFs; (i) Benicar launch expected in April-17 (expected to be a crowded market).

Monetization of investment in niche are as still sometime away: We believe increase in competition in Abilify coupled with high R&D expense and rise in depreciation due to planned capex of INR15b over the next 2-3 years will keep profit growth under check. We see limited room for upside from current levels as the stock trades at 27x/21x FY17E/18E PER. We maintain our Neutral rating with a target price of INR640 (20x FY18E EPS).

Y/E March		FY1	16			FY:	7		FY16	FY17E	FY17	7F
- Indicit									11120	111/2		
	10	2Q	3Q	4Q	1Q	2Q	3QE	4QE			2QE	vs Est
Net Sales	5,833	10,033	9,210	6,256	7,270	8,716	8,075	7,824	31,453	31,885	7,844	11.1%
YoY Change (%)	18.0	83.7	80.3	24.7	24.6	-13.1	-12.3	25.1	68.8	1.4	-22.2	
EBITDA	1,021	3,748	3,839	1,423	1,559	1,771	1,696	1,670	10,025	6,696	1,694	4.5%
Margins (%)	17.5	37.4	41.7	22.7	21.4	20.3	21.0	21.3	31.9	21.0	21.6	
Depreciation	129	133	217	244	194	206	222	405	722	1,027	215	
Interest	5	7	10	13	11	10	3	-11	37	12	3	
Other Income	0	10	28	26	14	12	85	208	91	319	70	
PBT	886	3,618	3,640	1,192	1,369	1,567	1,556	1,484	9,357	5,975	1,546	
Tax	188	737	951	286	333	332	350	300	1,986	1,315	375	
Rate (%)	21.2	20.4	26.1	24.0	24.3	21.2	22.5	20.2	21.2	22.0	24.3	
Minority Interest & Profit/Loss of Asso. (1	-1	-1	-5	16	49	-1	-5	6	-2	4	
Reported PAT	698	2,882	2,690	911	1,020	1,187	1,207	1,188	7,365	4,662	1,168	1.6%
Adj PAT	698	2,882	2,690	911	1,020	1,187	1,207	1,188	7,365	4,662	1,168	1.6%
YoY Change (%)	7.9	273.1	280.7	29.5	46.2	-58.8	-55.1	30.5	212.8	-36.7	-59.5	
Margins (%)	12.0	28.7	29.2	14.6	14.0	13.6	14.9	15.2	23.4	14.6	14.9	

E: MOSL Estimates

Kumar Saurabh (Kumar Saurabh@Motilal Oswal.com); +91 22 6129 1519

Gaurav Tinani (Gaurav.Tinani@motilaloswal.com); +91 22 6129 1552

Investors are advised to refer through important disclosures made at the last page of the Research Report.

Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital. MOTILAL OSWAL Alembic Pharmaceuticals

Key highlights

India formulations (41% of sales): India's branded formulation grew 17.2%YoY to INR3.6b. ALPM's acute segment witnessed strong 22%YoY growth after being impacted by external factors like FDC ban and NLEM in 1QFY17. The specialty segment grew 16%YoY in 2QFY17. Cardiology business witnessed 17%YoY growth for the quarter, while the Anti-diabetic & Gynecology were grew 28%YoY and 34%YoY respectively. With increased focus on specialty products and improving MR productivity (MR's: 5,000), we model 15% CAGR growth over FY16-18E for domestic business. The company currently has ~170-180 products and plans to launch 20-25 new products every year.

Exhibit 1: Sales decline 13% YoY



Exhibit 2: India branded business witnessed strong growth

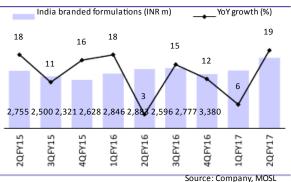


Exhibit 3: Acute led growth in domestic formulation business (Sep 16)

		Market	Alembic gr	owth (%)
Therapies	Market Share (%)	growth (%)	Secondary (ORG-IMS)	Primary
CVS	2.09	8	20	17
Anti-Diabetic	1.84	16	43	28
Gynecology	2.91	7	25	34
Gastrology	1.88	11	-2	0
Dermatology	0.4	15	-8	9
Orthopedic	0.96	9	4	10
Ophthalmology	1.41	11	14	1
Nephro/URO	2.14	14	19	22
Anti-Infective	2.74	23	10	16
Cold & Cough	4.83	36	27	35
Overall	1.62	14	5	19

International business grew 40%YoY to

INR3.5b, primarily led by higher sales in the US. 23 products have been launched by Alembic USA under its own brand. Sequential increase in international business is also attributed to increase in market share of Abilify and launch of existing products under own front-end (23 in last 12M). Alembic has 33 pending ANDAs with ~40% as Para IV/ FTF fillings. The company expects 6-8 ANDA approvals in 2HFY17.

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International Generics (40% of sales):

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Exhibit 4: Key operating metrics

	2QFY14 30	QFY14 4QF	Y14 1QFY1	5 2QFY15	3QFY15 4	QFY15 1Q	FY16 2QFY	16 3QFY1	6 4QFY16	1QFY17 20	QFY17		
Revenue Mix (%)													
India	56.4	52.2	49.0	50.1	56.1	55.0	52.0	49.4	30.4	33.1	43.8	40.6	41.3
Exports (B+G)	26.3	31.3	33.2	27.5	25.9	28.5	30.9	29.8	56.1	56.0	30.0	41.9	41.9
APIs	16.0	15.5	17.4	21.4	17.1	15.8	16.8	19.8	13.5	10.9	26.3	17.4	18.7
Revenue Gr. (%)	19.7	30.8	22.9	15.0	12.5	5.8	9.2	19.0	85.4	80.7	25.0	24.6	(13.6)
India	8.3	11.5	9.9	12.3	12.0	11.5	15.8	17.2	0.6	8.9	5.2	2.6	17.2
Exports (B+G)	114.5	100.2	70.4	35.9	10.8	(3.6)	1.8	29.0	302.3	255.1	21.2	75.2	(38.3)
APIs	(14.0)	12.9	2.8	(0.7)	19.7	7.5	5.4	9.9	46.6	24.5	95.8	9.7	19.5
Cost of sales (%)	80.9	79.0	80.3	80.6	80.3	80.1	80.6	82.5	62.6	58.3	77.3	78.6	79.7
Raw material	39.0	36.1	38.0	35.8	34.7	34.1	34.6	36.5	22.6	22.4	19.8	26.3	27.5
Staff cost	12.2	13.2	14.5	15.3	14.1	15.5	15.0	15.1	11.9	12.7	15.5	16.0	13.6
R&D cost	6.9	6.0	6.7	6.0	5.7	6.0	6.1	8.2	7.8	7.6	17.8	10.9	12.5
Other expenses	22.8	23.7	21.2	23.5	25.9	24.5	24.9	22.7	20.5	15.6	24.2	25.4	26.1
TaxRate	23.4	25.8	24.1	23.9	19.3	21.5	20.7	21.2	20.4	26.1	24.0	24.3	21.2
Margins (%)													
Gross Margins	61.0	63.9	62.0	64.2	65.3	65.9	65.4	63.5	77.4	77.6	80.2	73.7	72.5
EBITDA Margins	19.1	21.0	19.7	19.4	19.7	19.9	19.4	17.5	37.4	41.7	22.7	21.4	20.3
EBIT Margins	17.0	19.0	17.3	17.3	17.7	17.6	17.2	15.3	36.0	39.3	18.8	18.8	18.0
PAT margins	12.7	13.6	13.2	13.1	14.1	13.8	14.0	12.0	28.7	29.2	14.6	14.0	13.6
											Source: (Company	; MOSL

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Valuation and view

We believe that ALPM's business profile has undergone a transformation led by renewed efforts by management team to invigorate domestic growth and rapid expansion in export front. This has resulted in marked improvement in profitability and return ratios, likely to sustain over medium term and the re-rating undergone over the past 18 months does reflect this improvement.

With increased earnings growth visibility and strengthening balance sheet, we ascribe a PE multiple of 20x, which is at par with the sector average noting healthy balance sheet, strong return ratios and high earnings growth.

However, we don't see further room for re-rating from current levels as the company is already trading at 27x/21x on FY17E/FY18E earnings, in line with the sector average. We maintain our Neutral rating, based on stretched valuation, with a target of 640 based on 20x FY18E.

Key catalysts to drive stock's performance over the medium term are:

- Ramp-up of own front-end operations in US and its execution on key launches
- Continued improvement in domestic product mix in favour of chronic/specialty segments which would help outperform industry growth rates
- Improved free cash flow generation

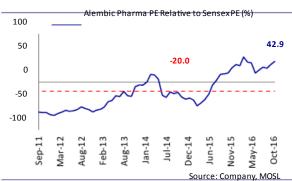
Key risks to our investment thesis:

- Regulatory delays affecting key US launches,
- Any adverse US FDA action upon inspection of its US facilities
- Increased coverage of DPCO impacting domestic business (price erosion).





Exhibit 6: ALPM trades at 43% premium to Sensex PE



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Story in charts

Exhibit 7: Top line growth to come down due to higher base

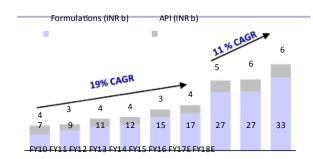
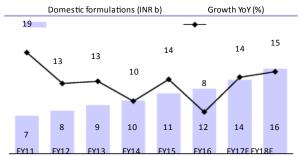


Exhibit 8: Specialty therapies to drive domestic growth



Source: Company, MOSL

Source: Company, MOSL

Source: Company, MOSL

Exhibit 9: Pick up in R&D expense

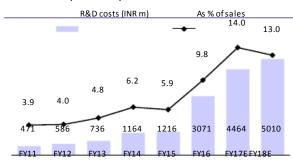
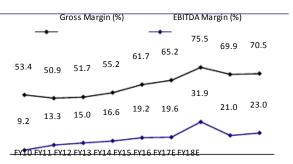


Exhibit 10: Better business mix to yield margin expansion



Source: Company, MOSL

Exhibit 11: EPS growth to slow down

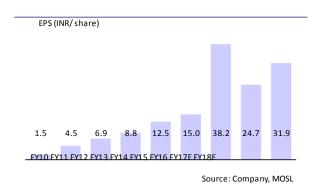
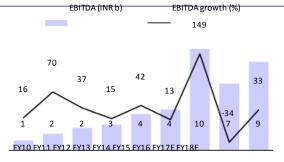


Exhibit 12: EBITDA improved over the years



Source: Company, MOSL

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Financials and valuations

Consolidated - Income Statement							(INR	Million)
Y/E March	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E
Net Sales	14,654	15,204	18,632	20,527	31,453	31,885	38,535	45,061
Change (%)	21.9	3.7	22.6	10.2	53.2	1.4	20.9	16.9
EBITDA	2,194	2,520	3,577	4,026	10,025	6,696	8,863	10,815
Margin (%)	15.0	16.6	19.2	19.6	31.9	21.0	23.0	24.0
Depreciation	337	350	405	444	722	1,027	1,378	1,814
EBIT	1,858	2,170	3,172	3,582	9,303	5,668	7,485	9,000
Int. and Finance Charges	376	240	104	18	37	12	10	C
Other Income - Rec.	128	133	38	26	91	319	347	406
PBT bef. EO Exp.	1,610	2,063	3,106	3,591	9,357	5,975	7,821	9,406
PBT after EO Exp.	1,610	2,063	3,106	3,591	9,357	5,975	7,821	9,406
Current Tax	312	401	685	764	1,986	1,315	1,799	2,257
Deferred Tax	-4	10	66	0	174	0	0	C
Tax Rate (%)	19.2	19.9	24.2	21.3	23.1	22.0	23.0	24.0
Reported PAT	1,301	1,653	2,355	2,827	7,197	4,661	6,022	7,149
PAT Adj for EO items	1,301	1,653	2,355	2,827	4,821	4,661	6,022	7,149
Change (%)	52.4	27.0	42.5	20.0	70.5	-3.3	29.2	18.7
Margin (%)	8.9	10.9	12.6	13.8	15.3	14.6	15.6	15.9
Consolidated - Balance Sheet								
Y/E March	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E
Equity Share Capital	377	377	377	377	377	377	377	377
Total Reserves	3,573	4,652	6,379	8,469	15,628	19,156	24,049	30,068
Preference Capital	0	0	0	0	0	0	0	Ć
Net Worth	3,950	5,029	6,756	8,846	16,005	19,533	24,426	30,445
Deferred Liabilities	95	139	227	314	501	501	501	501
Total Loans	3,527	1,868	1,238	2,385	1,325	1,125	925	725
Capital Employed	7,572	7,036	8,221	11,546	17,832	21,159	25,852	31,671
Gross Block	4,629	5,725	6,541	8,756	11,190	17,190	22,190	26,190
Less: Accum. Deprn.	1,951	2,283	2,688	3,132	3,878	4,906	6,284	8,098
Net Fixed Assets	2,678	3,442	3,854	5,978	7,748	12,720	16,342	18,528
Capital WIP	582	323	323	323	925	319	385	451
Total Investments	33	33	34	23	21	21	21	21
Curr. Assets, Loans&Adv.	7,226	6,680	7,968	10,089	15,900	13,850	15,726	20,140
Inventory	2,587	2,668	3,108	3,828	5,776	4,733	5,606	6,444
Account Receivables	1,993	2,329	2,734	3,612	3,505	3,553	4,294	5,021
Cash and Bank Balance	471	161	240	268	4,508	3,424	3,240	5,651
Loans and Advances	2,174	1,522	1,887	2,381	2,111	2,140	2,586	3,024
Curr. Liability & Prov.	2,947	3,442	3,957	4,866	6,762	5,751	6,623	7,469
Account Payables	2,092	2,400	2,884	3,109	5,664	3,813	4,516	5,191
Other Current Liabilities	499	419	339	715	656	665	803	939
Provisions	357	623	734	1,042	443	1,273	1,303	1,338
Net Current Assets	4,279	3,239	4,011	5,223	9,138	8,099	9,104	12,672
Misc Expenditure	0	0	0	0	0	0	0	,
Appl. of Funds	7,572	7,036	8,221	11,546	17,832	21,159	25,852	31,671
E: MOSL Estimates; * Adjusted for treasury stoc		•	•	•				

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Financials and valuations

Ratios								
Y/E March	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E
Basic (INR)								
EP\$	6.9	8.8	12.5	15.0	38.2	24.7	31.9	37.9
Cash EPS	8.7	10.6	14.6	17.4	29.4	30.2	39.3	47.5
BV/Share	21.0	26.7	35.8	46.9	84.9	103.6	129.6	161.5
DPS	1.4	2.5	3.0	3.5	4.0	5.0	5.0	5.0
Payout (%)	23.6	33.4	28.1	28.1	12.6	24.3	18.8	15.9
Valuation (x)								
P/E	97.5	76.8	53.9	44.9	17.6	27.2	21.1	17.7
Cash P/E	77.5	63.4	46.0	38.8	22.9	22.3	17.1	14.2
P/BV	32.1	25.2	18.8	14.3	7.9	6.5	5.2	4.2
EV/Sales	8.9	8.5	6.9	6.3	3.9	3.9	3.2	2.7
EV/EBITDA	59.2	51.0	35.7	32.0	12.3	18.6	14.1	11.3
Dividend Yield (%)	0.2	0.4	0.4	0.5	0.6	0.7	0.7	0.7
Return Ratios (%)								
RoE	37.6	36.8	40.0	36.3	38.8	26.2	27.4	26.1
RoCE	23.4	25.7	32.7	29.6	50.6	24.6	26.2	25.3
RoIC	24.2	26.7	34.0	30.4	61.4	29.7	29.1	28.6
Working Capital Ratios								
Asset Turnover (x)	1.9	2.2	2.3	1.8	1.8	1.5	1.5	1.4
Inventory (Days)	64	64	61	68	67	54	53	52
Debtor (Days)	49	56	53	64	40	40	40	40
Creditor (Days)	52	58	57	55	66	44	43	42
Leverage Ratio (x)								
Interest Cover Ratio	5	9	31	201	253	463	730	NA
Debt/Equity	0.9	0.4	0.2	0.3	0.1	0.1	0.0	0.0
* Adjusted for treasury stocks								
Consolidated - Cash Flow Statement								
Y/E March	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E
Net Profit / (Loss) Before Tax	1,610	2,064	3,106	3,591	9,357	5,975	7,821	9,406
Depreciation	337	350	405	444	722	1,027	1,378	1,814
Interest & Finance Charges	262	146	66	-9	-54	-307	-337	-406
Direct Taxes Paid	327	387	663	676	1,973	1,315	1,799	2,257
(Inc)/Dec in WC	-616	439	-694	-1,184	325	-46	-1,188	-1,157
CF from Operations	1,265	2,611	2,221	2,166	8,378	5,336	5,876	7,400
CF from Operating incl EO	1,418	2,648	2,256	1,869	9,209	5,163	5,703	7,227
(inc)/dec in FA	-612	-854	-816	-2,215	-3,037	-5,394	-5,066	-4,065
Free Cash Flow	806	1,794	1,440	-346	6,172	-231	636	3,162
(Pur)/Sale of Investments	0	0	0	0	0	0	0	C
Others	48	184	37	37	93	319	347	406
CF from Investments	-564	-670	-779	-2,178	-2,944	-5,075	-4,720	-3,660
(Inc)/Dec in Debt	143	-1,696	-633	1,149	-1,058	-199	-195	-195
Interest Paid	-372	-288	-104	-18	-37	-12	-10	C
Dividend Paid	-216	-304	-662	-794	-908	-1,134	-1,134	-1,134
CF from Fin. Activity	-446	-2,288	-1,398	337	-2,003	-1,345	-1,340	-1,329
Inc/Dec of Cash	408	-310	79	28	4,262	-1,257	-357	2,238
Add: Beginning Balance	63	471	161	240	246	4,681	3,597	3,413
				268				

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Corporate profile

Company description

Started in 1907, Alembic Pharma (ALPM) is one of the oldest pharmaceutical companies of Indian origin in the domestic formulations market. The company was first established as a tincture and alcohol manufacturer and made its way into modern medicine in 1940. Today ALPM is being run by its fourth generation of entrepreneurs, is the 25th largest formulations player in India and has sales presence in more than 75 countries.

Exhibit 13: Sensex rebased



Exhibit 14: Shareholding pattern (%)

	Sep-16	Jun-16	Sep-15		
Promoter	74.4	74.1	74.1		
DII	2.9	2.7	4.9		
FII	10.9	10.9	7.7		
Others	11.9	12.3	13.3		
Note: FII Includes depository receipts					

Exhibit 15: Top holders

Holder Name	% Holding
-	

Exhibit 16: Top management

Name	Designation
Chirayu R Amin	Chairman and MD & CEO
Pranav Amin	Joint Managing Director
Shaunak Amin	Joint Managing Director
Rajkumar Baheti	Director & CFO
Ajay Kumar Desai	Company Secretary

Exhibit 17: Directors

Name	Name
Chirayu R Amin	K G Ramanathan*
Pranav Amin	Milin Mehta*
Shaunak Amin	Paresh Saraiya*
Rajkumar Baheti	Pranav N Parikh*
Archana Hingorani*	
	*Independent

Exhibit 18: Auditors

Name	Туре	
H R Kapadia	Cost Auditor	
K S Aiyar & Co	Statutory	
Samdani Shah & Associates	Secretarial Audit	
Sharp & Tannan	Internal	

Exhibit 19: MOSL forecast v/s consensus

EPS (INR)	MOSL forecast	Consensus forecast	Variation (%)
FY17	24.7	23.3	6.0
FY18	31.9	30.2	5.9

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NOTES

25 October 2016

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Varun.kumar@motilaloswal.com Contact : (+65) 68189232

Office Address:21 (Suite 31),16 Collyer Quay,Singapore 04931

Kadambari Balachandran kadambari.balachandran@motilaloswal.com (+65) 68189233 / 65249115



Phone: +91 22 3982 5500 E-mail: reports@motilaloswal.com 25 October 2016

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