

### Strong beat on operational performance

Ajanta Pharma reported stellar Q2 beating our estimates on the operating performance. Top-line grew 8% YoY, in-line with our estimate, driven by US and branded Africa business. Other geographies including India were muted. However, lower opex aided margins at 38.3% (up 490 bps QoQ and 1,070 bps YoY), way higher than our estimates. While the same is expected to taper as activities resume in subsequent quarters, management re-iterated its guidance of EBITDA margins at 29-30% for FY21E.

Higher EBITDA, better working capital management and end of the capex cycle contributed to Rs2.4bn FCF in 1HFY21 (Rs2bn in FY20). Ajanta announced buyback of Rs1.35bn (~Rs4.5bn cash on books).

Ajanta has invested Rs16bn in facilities over the last 4-years, majority of which has completed, indicating better free cash generation going ahead. We reckon that peak capacity utilization at Guwahati and Pithampur plants over the next 2 years could potentially add Rs12bn to revenues. We estimate sales/PAT CAGR of 14%/15% over FY21–23E, along with a margin sustenance at 28-29%.

We maintain our estimates and introduce FY23 in this note. At the CMP, Ajanta is trading at 22x and 19x its FY22E and FY23E EPS, respectively. Maintain ACCUMULATE. Volatility in the emerging markets remains a key risk.

#### Key commentary from the management:

**Guidance:** Branded business (Africa and Asia) is expected to grow 8-9%, US by 20%, while India is guided for a de-growth of 5% (lockdown impacting its 40% acute portfolio) implying a top-line growth of 5%. Nonetheless, given the lower on-field activities company guided for 29-30% EBITDA margin for FY21E. Gross margins guided at 75-76% as inventory costs will shoot up in 2H.

#### Q2FY21 Result (Rs Mn)

Particulars	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)
Revenue	7,159	6,428	11.4	6,682	7.1
Total Expense	4,417	4,651	(5.0)	4,450	(0.7)
EBITDA	2,743	1,776	54.4	2,232	22.9
Depreciation	283	233	21.6	280	1.1
EBIT	2,459	1,543	59.3	1,952	26.0
Other Income	49	132	(63.3)	131	(63.0)
Interest	15	49	(69.0)	16	(6.1)
EBT	2,492	1,626	53.3	2,067	20.6
Tax	790	452	74.8	589	34.1
RPAT	1,702	1,174	45.0	1,478	15.2
APAT	1,702	1,174	45.0	1,478	15.2
			(bps)		(bps)
Gross Margin (%)	78.3	74.1	420	77.1	121
EBITDA Margin (%)	38.3	27.6	1067	33.4	490
NPM (%)	23.8	18.3	551	22.1	166
Tax Rate (%)	31.7	27.8	391	28.5	319
EBIT Margin (%)	34.4	24.0	1034	29.2	514

CMP	Rs 1,611
Target / Upside	Rs 1,771 / 10%
NIFTY	12,120

#### Scrip Details

Equity / FV	Rs 175mn / Rs 2
Market Cap	Rs 141bn
	USD 2bn
52-week High/Low	Rs 1,760/ 942
Avg. Volume (no)	1,81,153
Bloom Code	AJP IN

Price Performance	1M	3M	12M
Absolute (%)	1	(5)	61
Rel to NIFTY (%)	(5)	(14)	58

#### Shareholding Pattern

	Mar'20	Jun'20	Sep'20
Promoters*	70.5	70.5	70.5
MF/Banks/FIs	9.4	9.7	10.1
FIIIs	8.9	8.2	7.7
Public / Others	11.2	11.6	11.7

#### Valuation (x)

	FY21E	FY22E	FY23E
P/E	25.0	22.1	18.8
EV/EBITDA	17.0	14.7	12.2
ROE (%)	20.1	19.6	19.7
RoACE (%)	18.8	18.3	18.6

#### Estimates (Rs mn)

	FY21E	FY22E	FY23E
Revenue	27,214	30,983	35,033
EBITDA	7,972	8,906	10,345
PAT	5,656	6,400	7,524
EPS (Rs.)	64.5	73.0	85.8

Note: \*Promoters Pledge Shares as on Sep'20 is 11.32%

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**Exhibit 1: Revenue mix**

Rs mn	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	1HFY21	1HFY20	YoY (%)	FY21	FY20	YoY (%)
Domestic Formulations	2,030	2,030	0.0	1,740	16.7	3,770	3,970	(5.0)	7,313	7,690	(4.9)
US	1,540	1,110	38.7	1,490	3.4	3,030	2,130	42.3	6,391	5,160	23.9
Africa branded	1,120	820	36.6	1,080	3.7	2,200	1,740	26.4	3,769	3,490	8.0
Africa Tender	510	720	(29.2)	620	(17.7)	1,130	1,530	(26.1)	2,074	2,440	(15.0)
Asia	1,800	1,810	(0.6)	1,610	11.8	3,410	3,070	11.1	7,268	6,730	8.0
Others	30	20	50.0	30	0.0	60	50	20.0	88	80	10.0
Gross revenues	7,030	6,510	8.0	6,570	7.0	13,600	12,490	8.9	26,904	25,590	5.1

Source: Company, DART

### Key Concall Highlights

- India:** Q2 reported a flattish performance YoY, 16% QoQ. While chronic business has seen revival, the lower offtake of ophthalmic and derma products due to lower clinic footfalls continue to impact growth. The cardiac segment also faced slowdown and grew 10% vs IPM growth of 13%. However, pain segment grew 8% YoY vs IPM of 1%. With Ajanta being the 3<sup>rd</sup> largest player in its covered ophthalmology market, it expects growth to peak in the medium term for this segment. However, derma has been sluggish for some time now and is expected to remain subdued given the higher concentration of cosmetology products. While the MR activity on field has resumed normalcy, most marketing and promotional activities are yet to resume fully. We project India formulations to report decline of 5% and the same is expected to recover to 11% in FY22E.
- US:** Ajanta continue to report healthy growth in the US (39% YoY; 32% growth YoY in US\$ terms) aided by currency, new launches and market share gains. The management lowered its filing guidance of 3-4 (vs 10-12) but maintained 7-8 launches for FY21E (8 launches in 1H). We expect the US business to grow 22% sales CAGR over FY20-22E, led by new launches and a lower base. On a cumulative basis, Ajanta has 33 approvals, and 19 products pending for approval.
- Asia:** The Asia business reported flattish performance YoY but recovered to 12% growth QoQ. Management guided for normalcy in these markets from 4Q onwards as 2<sup>nd</sup> wave of COVID is resulting into pre-buying. As on FY20, Asia has 350+ products registered, 15 new launches in 7 major markets.
- Africa:** Strong growth in the branded business continues led by strong pull back factor of brands. Further, the tender business declined 29% YoY and 18% QoQ in-line with expectation. We expect branded Africa business to report 9% CAGR, while the tender business is expected to decline 2% over FY20-23E.
- Capex:** Ajanta's Dahej facility, built with a capex of ~Rs4bn, is expected to ramp up from FY22E. The management guided for capex of Rs1.5bn for FY21. Most of the capex would be spent on the Pithampur facility. With majority of capex done, management guided for operating leverage to drive profitability in the next 2-3 years.

**Profit and Loss Account**

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
<b>Revenue</b>	<b>25,879</b>	<b>27,214</b>	<b>30,983</b>	<b>35,033</b>
<b>Total Expense</b>	<b>19,045</b>	<b>19,242</b>	<b>22,077</b>	<b>24,688</b>
COGS	6,557	6,774	7,711	8,644
Employees Cost	4,856	5,112	5,978	6,764
Other expenses	7,632	7,356	8,388	9,280
<b>EBIDTA</b>	<b>6,833</b>	<b>7,972</b>	<b>8,906</b>	<b>10,345</b>
Depreciation	957	940	1,136	1,186
<b>EBIT</b>	<b>5,876</b>	<b>7,032</b>	<b>7,770</b>	<b>9,159</b>
Interest	119	79	35	31
Other Income	922	902	913	926
Exc. / E.O. items	0	0	0	0
<b>EBT</b>	<b>6,679</b>	<b>7,855</b>	<b>8,648</b>	<b>10,054</b>
Tax	1,963	2,199	2,248	2,531
RPAT	4,716	5,656	6,400	7,524
Minority Interest	0	0	0	0
<b>Profit/Loss share of associates</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>APAT</b>	<b>4,716</b>	<b>5,656</b>	<b>6,400</b>	<b>7,524</b>

**Balance Sheet**

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
<b>Sources of Funds</b>				
Equity Capital	175	175	175	175
Minority Interest	0	0	0	0
Reserves & Surplus	25,813	30,022	34,975	41,051
<b>Net Worth</b>	<b>25,989</b>	<b>30,197</b>	<b>35,150</b>	<b>41,227</b>
Total Debt	436	437	437	438
Net Deferred Tax Liability	1,897	1,951	2,030	2,156
<b>Total Capital Employed</b>	<b>28,321</b>	<b>32,586</b>	<b>37,617</b>	<b>43,821</b>

**Applications of Funds**

Net Block	<b>13,813</b>	<b>14,479</b>	<b>14,343</b>	<b>14,479</b>
CWIP	2,227	2,327	2,627	2,927
Investments	181	221	268	328
<b>Current Assets, Loans &amp; Advances</b>	<b>16,966</b>	<b>19,897</b>	<b>24,934</b>	<b>30,935</b>
Inventories	4,957	4,840	5,071	5,502
Receivables	7,753	7,371	7,475	8,173
Cash and Bank Balances	2,053	5,403	10,004	14,762
Loans and Advances	669	749	850	965
Other Current Assets	863	863	863	863
<b>Less: Current Liabilities &amp; Provisions</b>	<b>4,866</b>	<b>4,338</b>	<b>4,555</b>	<b>4,848</b>
Payables	3,623	3,159	3,295	3,518
Other Current Liabilities	1,242	1,179	1,260	1,330
<i>sub total</i>				
Net Current Assets	12,100	15,559	20,379	26,087
<b>Total Assets</b>	<b>28,321</b>	<b>32,586</b>	<b>37,617</b>	<b>43,821</b>

E – Estimates

**Important Ratios**

Particulars	FY20A	FY21E	FY22E	FY23E
<b>(A) Margins (%)</b>				
Gross Profit Margin	74.7	75.1	75.1	75.3
EBIDTA Margin	26.4	29.3	28.7	29.5
EBIT Margin	22.7	25.8	25.1	26.1
Tax rate	29.4	28.0	26.0	25.2
Net Profit Margin	18.2	20.8	20.7	21.5
<b>(B) As Percentage of Net Sales (%)</b>				
COGS	25.3	24.9	24.9	24.7
Employee	18.8	18.8	19.3	19.3
Other	29.5	27.0	27.1	26.5
<b>(C) Measure of Financial Status</b>				
Gross Debt / Equity	0.0	0.0	0.0	0.0
Interest Coverage	49.3	89.5	222.0	298.5
Inventory days	70	65	60	57
Debtors days	109	99	88	85
Average Cost of Debt	30.7	18.0	8.0	7.0
Payable days	51	42	39	37
Working Capital days	171	209	240	272
FA T/O	1.9	1.9	2.2	2.4
<b>(D) Measures of Investment</b>				
AEPS (Rs)	53.8	64.5	73.0	85.8
CEPS (Rs)	64.7	75.2	85.9	99.3
DPS (Rs)	13.2	16.5	16.5	16.5
Dividend Payout (%)	24.6	25.6	22.6	19.2
BVPS (Rs)	296.3	344.3	400.8	470.1
RoANW (%)	19.5	20.1	19.6	19.7
RoACE (%)	18.6	18.8	18.3	18.6
RoAIC (%)	24.0	26.3	28.4	32.3
<b>(E) Valuation Ratios</b>				
CMP (Rs)	1611	1611	1611	1611
P/E	30.0	25.0	22.1	18.8
Mcap (Rs Mn)	1,41,324	1,41,324	1,41,324	1,41,324
MCap/ Sales	5.5	5.2	4.6	4.0
EV	1,39,036	1,35,686	1,31,087	1,26,329
EV/Sales	5.4	5.0	4.2	3.6
EV/EBITDA	20.3	17.0	14.7	12.2
P/BV	5.4	4.7	4.0	3.4
Dividend Yield (%)	0.8	1.0	1.0	1.0
<b>(F) Growth Rate (%)</b>				
Revenue	25.9	5.2	13.9	13.1
EBITDA	20.6	16.7	11.7	16.2
EBIT	18.9	19.7	10.5	17.9
PBT	29.9	17.6	10.1	16.3
APAT	21.9	19.9	13.1	17.6
EPS	21.9	19.9	13.1	17.6
<b>Cash Flow</b>				
<b>(Rs Mn)</b>	<b>FY20A</b>	<b>FY21E</b>	<b>FY22E</b>	<b>FY23E</b>
CFO	4,710	6,621	7,429	7,916
CFI	(2,617)	(1,745)	(1,348)	(1,681)
CFF	(1,045)	(1,524)	(1,481)	(1,476)
FCFF	2,093	4,875	6,081	6,234
Opening Cash	1,005	2,053	5,403	10,004
Closing Cash	2,053	5,403	10,004	14,762

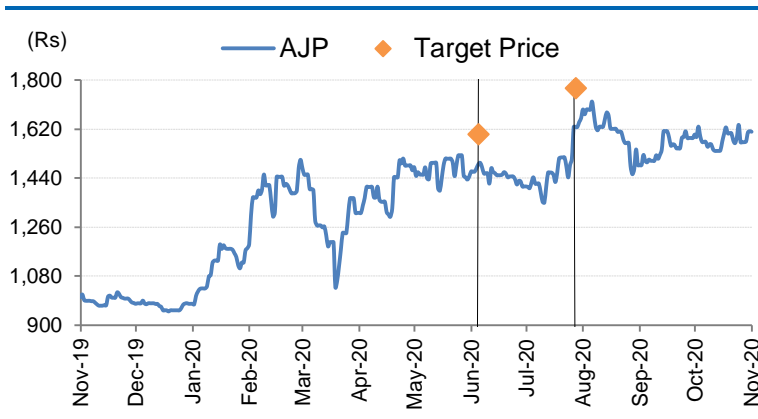
E – Estimates

### DART RATING MATRIX

Total Return Expectation (12 Months)

<b>Buy</b>	<b>&gt; 20%</b>
<b>Accumulate</b>	<b>10 to 20%</b>
<b>Reduce</b>	<b>0 to 10%</b>
<b>Sell</b>	<b>&lt; 0%</b>

### Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Jun-20	Accumulate	1,600	1,492
Aug-20	Accumulate	1,771	1,629

\*Price as on recommendation date

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