



3R MATRIX

	+	=	-
Right Sector (RS)	✓	■	■
Right Quality (RQ)	✓	■	■
Right Valuation (RV)	✓	■	■
+ Positive = Neutral - Negative			

Reco/View

Reco: Buy	↔
CMP: Rs. 319	
Price Target: Rs. 385	↑
↑ Upgrade ↔ Maintain ↓ Downgrade	

Company details

Market cap:	Rs. 17,109 cr
52-week high/low:	Rs. 345/62
NSE volume: (No of shares)	24.8 lakh
BSE code:	540222
NSE code:	LAURUSLABS
Free float: (No of shares)	38.1 cr

Shareholding (%)

Promoters	28.8
FII	22.8
DII	6.3
Others	42.1

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	11.1	101.7	211.3	338.1
Relative to Sensex	7.1	96.7	193.8	339.2

Sharekhan Research, Bloomberg

Summary

- Q2FY2021 was yet another quarter of stellar performance for Laurus Labs (Laurus) with results beating estimates on all parameters. Sales grew 60% yoy while adjusted PAT jumped 331% yoy.
- The formulations business is witnessing elevated traction, which is expected to sustain going ahead. Also Laurus is expanding its formulations capacities by 80% over FY21&FY22 to support growth.
- Synthesis and API segments are on track for a double digit growth. Operating leverage, favorable mix to support OPM expansion.
- Strong growth prospects, visibility on earnings, healthy balance sheet and return ratios are key positives We retain a Buy recommendation with a revised PT of Rs 385.

Q2FY2021 was yet another stellar quarter for Laurus Labs Ltd (Laurus). Sales stood at Rs. 1138.8 crore, translating to a sturdy rise of 60% y-o-y on the back of robust growth in the lucrative formulations business and a double digit growth in the generic API's. Operating margins surprised positively, surging 1351 bps y-o-y to 32.8%, aided by an expansion in the gross margins, benefits of operating leverage. Operating profit grew sharply by 171.9% y-o-y to Rs. 373 crore. PAT stood at Rs. 241.7 crores as compared to Rs 56 crores in corresponding quarter and was ahead of estimates. Robust growth in the formulations business and emerging opportunities in the API space coupled with strong order book for the synthesis business, which will unfold over the near to medium term, provides ample growth visibility. Moreover, almost doubling of capacity, primarily to cater to the surge in demand for formulations augurs well and would substantially boost revenues. Laurus had revised its capex guidance upwards to Rs 1200 crore over FY2021 and FY2022, which provides ample visibility on growth going ahead. The other API business is also likely to grow on the back of new product launches. The generic API segment could also benefit from the emerging opportunities. Higher share of the formulations business would lead to improved product mix and would help margins expansion. The robust performance in the quarter points at a strong growth trajectory going ahead for the company. We expect the company to report a sales and adjusted profit CAGR of 26% and 55%, respectively, over FY2020-FY2023.

Key Positives

- Strong 60% y-o-y growth in topline aided by a sturdy growth in the FDF (Formulations) businesses.
- Impressive operating performance with a 172% y-o-y rise in operating profit and a 1351 bps y-o-y expansion in operating margins to 32.8%.
- Gross margins at 56%, is the highest in the past 13 quarters

Key Negatives

- Share of revenues from the ARV-API business have declined from 51.4% to 33%.

Our Call

Retain Buy with a Revised PT of Rs 385: Q2FY2021 was yet another quarter of stellar performance. The strong growth trajectory is expected to sustain going ahead as well. The formulations business is witnessing elevated traction and the management is confident of sustaining the momentum going ahead. Further, Laurus is increasing its formulation capacity to cater to the surging demand. Overall the company has revised upwards its capex guidance to Rs 1200 cr over FY2021 and FY2022. This provides ample visibility on growth. The custom synthesis segment is also likely to grow in healthy double digits aided by new projects across various stages. The API business has gained good momentum and is expected to benefit from the emerging opportunities. Strong topline growth and OPM expansion would lead to a sturdy 56% earnings CAGR over FY2020-FY2023. Given the impressive margin performance in Q2FY2021, we have raised our estimates for FY22/FY23. At CMP, the stock is trading at a valuation of 21.6x/17.5x its FY2022E / FY2023E EPS. Strong topline growth prospects, visibility on earnings and a healthy return ratios and low debt-equity are the key positives. We retain Buy recommendation on the stock with a revised PT of Rs 385.

Key Risks

Any delay in product approvals or any negative outcome of facility inspection by the USFDA can affect earnings prospects.

Valuation (Consolidated)

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Sales	2291.9	2831.7	4011.9	4745.7	5637.9
Operating Profits	356.0	564.5	1103.3	1328.8	1589.9
OPM(%)	15.5	19.9	27.5	28.0	28.2
PAT	93.8	255.3	635.5	787.0	970.4
PATM (%)	4.1	9.0	15.8	16.6	17.2
EPS	1.8	4.8	11.9	14.8	18.2
P/E	181.6	66.7	26.8	21.6	17.5
EV/EBIDTA	50.9	31.9	16.3	13.3	11.0
ROE (%)	6.0	14.4	26.4	24.7	23.3
ROCE (%)	7.2	13.2	25.7	25.5	25.3

Source: Company; Sharekhan estimates

Note: We now convert Laurus labs into a Stock update; it was earlier a 'Viewpoint' under our coverage.

Stellar performance for the quarter: Laurus reported yet another quarter of stellar performance with results ahead of estimates. Sales at Rs 1138.8 cr grew steadily by 59.9% y-o-y on the back of 183% y-o-y growth in the generic FDF segment. The other segments – Synthesis and API have staged a growth of 36.5% and 22.3% y-o-y respectively. Operating profit grew sharply to Rs 373 crore as compared to 137 Cr in Q2FY20, up by 172% y-o-y. The operating margins surprised positively expanding by a stellar 1351 bps y-o-y to 32.8% and beating the estimates. OPM expansion could be attributable to expansion of 650 bps y-o-y in gross margins, benefits of operating leverage and a favourable mix. Tracking the strong operating performance the PAT for the quarter stood at Rs 241.7 cr, up by 331.2% y-o-y as compared to a Rs 56 cr in Q2FY20. The PAT was ahead of estimates.

Laurus to expand formulations capacity by 80% by FY2022: Laurus' formulations business has grown multifold and has exhibited strong traction. The revenues from the formulations business has grown impressively to Rs. 452 crore from Rs. 160 crore in the corresponding quarter. The tender business from the low and middle income countries (LMIC) is also on a strong footing and the company has a sturdy order book. Laurus is currently operating at close to optimum utilization levels. With a strong demand environment, the management anticipates capacity constraints going ahead. Consequently, it is expanding capacities, primarily through brownfield expansion. The first leg of de-bottlenecking is expected to be over by end of Q4FY2021 (would be done in two phases – 1st to go onstream by end of Q3FY2021; 2nd one by Q4FY2021) while the second leg of expansion would be done in two phases, which would go on stream by September 2021 and December 2021. Cumulatively, the formulations capacity would increase by 80% over the next 2 years. Laurus is eyeing a revenue potential of 1.5-2x from the new capacities. Also, traction from the North America and EU is expected to sustain going ahead and would aid topline growth.

Synthesis business to clock a double digit growth: The Synthesis segment revenues have grown by a stellar 36.5% for Q2FY2021 to Rs 116 crore. Going ahead, management sees the synthesis business to be one of the key growth drivers for the company. Growth in the synthesis business would be driven by new client additions and new product commercialisation. As of the quarter, total active projects stood at 49, and the company sees new client wins happening, which would take the active projects higher. Currently the company has commenced commercial supplies for 4 products. Going ahead, Laurus expects new commercialisation to increase, which would drive the segment's sales. Laurus has incorporated a wholly owned subsidiary to have increased focus and eventually dedicated R&D and Manufacturing facility for the synthesis business. The Synthesis segment sales are expected to clock a double digit 19% CAGR over FY2020-FY2023.

Q2FY2021 Concall Highlights:

Generic FDF: Revenues from the segment continued its strong growth trajectory and grew impressively by 183% y-o-y to Rs 452 crore. Growth in the quarter was led by higher sales from tender business in LMIC. The segment constituted 40% of the total quarterly sales. During the quarter, Laurus launched the TLE400 in LMIC markets, while it has launched TLE 400 and TLE 600 in the US. Further the company has received 8 final approvals and have received 8 tentative approvals.

Generic API: The segment sales grew by a healthy 22% y-o-y to Rs 571 crore, led by a strong 33.3% growth in the ARV API segment to Rs 379 crore. The oncology API and other API's grew by 43% and 18% y-o-y respectively.

Revenue Mix: As of Q2FY2021, around 50% of the revenues are from the API segment, 40% from the FDF and 10% from Synthesis. Going ahead, the company expects the mix to change slightly in favor of the synthesis segment. It expects 40% of revenues to come each from the API and FDF segment while the balance 20% would be constitute by the Synthesis business. This augurs well from a margin expansion perspective as Synthesis business commands higher margins.

ANDA filings: The company plans to file 8-10 ANDAs each year in the US. Till date, it has filed 26 ANDAs in the US along with 9 in Europe and 12 in Canada The company has also filed a total of 61 DMF's and 264 patents, off which it has been granted 130 patents.

Capex: Laurus has been significantly increased to Rs 1200 crore in anticipation of a surge in demand. Of the total capex 40% of the spends each would be towards enhancing the API and FDF capacities and the balance 20% would be towards Synthesis segment. The capex is expected to be funded internally.

Results					Rs cr	
Particulars	Q2FY21	Q2FY20	y-o-y (%)	Q1FY21	q-o-q (%)	
Total Sales	1,138.8	712.4	59.9	974.3	16.9	
Operating profit	373.3	137.3	171.9	277.8	34.4	
Other income	5.1	1.4	276.2	7.1	-27.8	
EBITDA	378.4	138.7	172.9	284.9	32.8	
Interest	13.7	25.6	-46.5	15.1	-9.6	
Depreciation	51.0	47.8	6.6	48.8	4.5	
PBT	313.8	65.3	380.6	220.9	42.0	
Taxes	72.0	9.2	681.4	49.7	45.0	
Adjusted PAT	241.7	56.1	331.2	171.2	41.2	
Margins			BPS		BPS	
OPM %	32.8	19.3	1,351	28.5	427	

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector view - Growth momentum to improve

Indian pharmaceutical companies are better placed to harness opportunities and clock healthy growth going ahead. Indian companies are among the most competitive ones globally and hold a sizeable market share in most developed as well as other markets. Moreover, other factors such as easing of pricing pressures (especially in US generics market), rise in product approvals and plant resolutions by the USFDA coupled with strong growth prospects in domestic markets and emerging opportunities in the API space would be the key growth drivers. This would be complemented by the strong capabilities developed by Indian companies (leading to a shift towards complex molecules, biosimilars) and commissioning of expanded capacities by select players over the medium term. Collectively, this indicates a strong growth potential going ahead for pharma companies

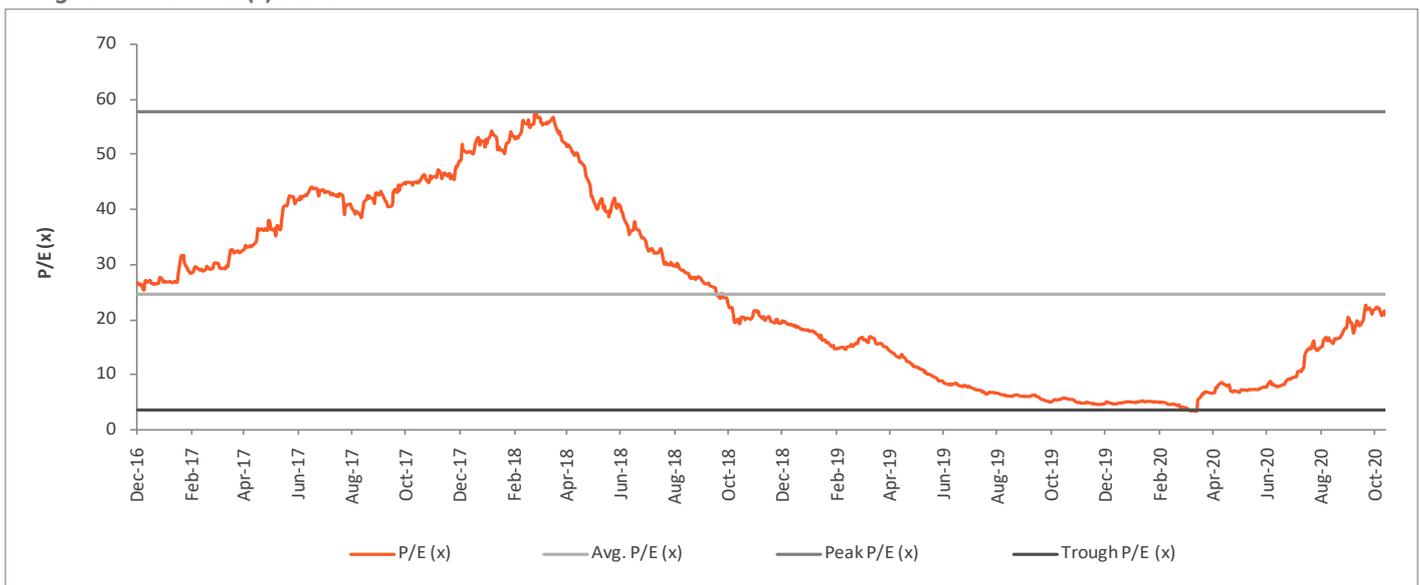
■ Company outlook - robust outlook

The formulations business is gaining traction with new approvals and launches. The company is enhancing its current portfolio, stepping up R&D activity and strengthening and expanding manufacturing capabilities. Further leveraging its strengths in the API segment, Laurus has forward-integrated into the lucrative formulations space and is now looking to increase its formulations capacities by 80% so as to cater to the surging demand. Sturdy growth in the formulations business in Q2FY2021 reflects the same and the management is confident of sustaining the strong growth momentum. Moreover, expected traction in the Synthesis business and improvement in the ARVs would be the key revenue drivers. Benefits of operating leverage and a favorable product mix would result in OPM expansion. Cumulatively, earnings are expected to grow by a 56% CAGR over FY2020-Fy2023.

■ Valuation - Retain Buy with a Revised PT of Rs 385

Q2FY2021 was yet another quarter of stellar performance. The strong growth trajectory is expected to sustain going ahead as well. The formulations business is witnessing elevated traction and the management is confident of sustaining the momentum going ahead. Further, Laurus is increasing its formulation capacity to cater to the surging demand. Overall the company has revised upwards its capex guidance to Rs 1200 cr over FY2021 and FY2022. This provides ample visibility on growth. The custom synthesis segment is also likely to grow in healthy double digits aided by new projects across various stages. The API business has gained good momentum and is expected to benefit from the emerging opportunities. Strong topline growth and OPM expansion would lead to a sturdy 56% earnings CAGR over FY2020-FY2023. Given the impressive margin performance in Q2FY2021, we have raised our estimates for FY22/FY23. At CMP, the stock is trading at a valuation of 21.6x/17.5x its FY2022E / FY2023E EPS. Strong topline growth prospects, visibility on earnings and a healthy return ratios and low debt-equity are the key positives. We retain Buy recommendation on the stock with a revised PT of Rs 385

One-year forward P/E (x) band



Source: Sharekhan Research

Peer valuation

Particulars	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)		EV/EBITDA (x)		RoE (%)	
				FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Laurus Labs	319.0	53.2	17,109.0	26.8	21.6	16.3	13.3	26.4	24.7
Granules India	384.0	24.7	9,508.0	17.2	14.8	11.1	9.1	23.7	22.1

Source: Company, Sharekhan Research

About company

Laurus is a leading research-driven pharmaceutical company, working with nine of the world's top 10 generic pharmaceutical companies in the world. Laurus sells APIs in 56 countries. The company's major focus areas include anti-retroviral, Hepatitis C, and Oncology drugs. Oncology is one of its core competencies, where it offers a comprehensive range of APIs in this segment. Laurus is continuously extending its portfolio by focusing on molecules in diabetes, ophthalmology, and cardio-vascular therapy areas. Laurus has four distinct business units, namely: Generics API, Generics FDF, Ingredients and Synthesis.

Investment theme

Built on strong capabilities in chemical development and manufacturing, Laurus has developed a wide range of in-house APIs and intermediates. Laurus is one of the world's leading suppliers of anti-retroviral APIs and intermediates. The company's low-cost technologies give it an edge over other players. Leveraging on API cost advantage for forward integration into generic formulations (FDF) and capitalising on leadership position in APIs (in key areas such as oncology, cardio-vascular, anti-diabetics, and ophthalmology) with foray into other regulated markets will drive the company's business over the next couple of years. Also the company's doubling its capacity to support the growth in the formulations business, which points towards a healthy growth going ahead.

Key Risks

- ◆ Slower-than-expected ramp-up in formulations or custom synthesis businesses.
- ◆ Reforms in the healthcare industry and uncertainty associated with pharmaceutical pricing, reimbursement and related matters could affect pricing and demand for Laurus' products.

Additional Data

Key management personnel

Dr. Satyanarayana Chava	Founder and CEO
Mr. V V Ravi Kumar	Executive Director and CFO
Dr. Lakshmana Rao C V	ED & Head, Quality
Mr. Krishna Chaitanya Chava	Corporate Development, Synthesis

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Ambit Capital	11.7
2	Amansa Holdings Pvt Ltd	6.1
3	Government Pension Global Fund	1.8
4	Vanguard Group Inc	1.2
5	Blackrock Inc	0.9
6	Norges Bank	0.9
7	HSBC Holdings	0.7
8	Kotak Mahindra Asset Management Co	0.7
9	UTI asset Management Co Ltd	0.6
10	ICICI Prudential Asset Management Co	0.6

Source: Bloomberg

Data as on 24 September 2020

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Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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