



3R MATRIX

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

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS	■	↔	■
RQ	■	↔	■
RV	■	↔	■

Reco/View

Reco: Buy	↔
CMP: Rs. 345	
Price Target: Rs. 410	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 18,523 cr
52-week high/low:	Rs. 386/62
NSE volume: (No of shares)	34.4 lakh
BSE code:	540222
NSE code:	LAURUSLABS
Free float: (No of shares)	38.2 cr

Shareholding (%)

Promoters	28.8
FII	22.8
DII	6.3
Others	42.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-0.2	4.7	126.1	294.1
Relative to Sensex	2.6	-11.8	104.5	281.7

Sharekhan Research, Bloomberg

Summary

- We retain Buy recommendation on the Laurus Labs Ltd (Laurus) with an unchanged PT of Rs 410.
- Q3FY2021 was yet another quarter of stellar performance with results ahead of estimates. The sales for the quarter were up 76% YoY, while adjusted PAT was up 274% YoY.
- Robust growth in the formulations business and emerging opportunities in the API space coupled with a strong order book for the synthesis business, provides ample growth visibility. Diversification in to non ARV space and synergies from Laurus Bio would be long term drivers.
- Strong topline growth prospects, visibility on earnings, healthy return ratios and low debt-equity are the key positives.

Q3FY2021 was yet another stellar quarter for Laurus Labs Ltd (Laurus). Sales stood at Rs. 1288 crore, translating to a sturdy rise of 76% y-o-y on the back of robust growth in the ARV – API segment and the formulations business. Operating margins surprised positively, surging 1281 bps y-o-y to 33%, aided by an expansion in the gross margins, benefits of operating leverage. Operating profit grew sharply by 188% y-o-y to Rs. 425 crores. PAT stood at Rs. 273 crores as compared to Rs 73 crores in the corresponding quarter and was ahead of estimates. Robust growth in the formulations business and emerging opportunities in the API space coupled with a 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 for the company. Over the long term, Laurus plans to diversify its presence in the non-ARV segments such as diabetics and cardiology and tap new markets so as to sustain the strong growth momentum. It has inked an agreement with a partner in the European markets for formulations. Further Synergies from Laurus Bio would also play out over the medium to long term and aid growth. 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 31% and 72%, respectively, over FY2020-FY2023.

Key positives

- Strong 76% y-o-y growth in topline aided by a sturdy growth in the ARV-API and FDF (Formulations) businesses.
- Impressive operating performance with a 188% y-o-y rise in operating profit and a 1280 bps y-o-y expansion in operating margins to 33%.
- Gross margins at 54.7%, expanded by 420 bps y-o-y.

Key negatives

- Share of revenues from the other-API business have remained flat on a y-o-y basis due to a change in the delivery schedules by a few customers.

Our Call

Retain Buy with PT of Rs 410: Q3FY2021 was yet another quarter of stellar performance. The strong growth trajectory is expected to sustain going ahead as well. The formulations business is well placed to harness the opportunities and the management is confident of sustaining the momentum going ahead. Further, Laurus is increasing its formulation capacity to cater to the surging demand. 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. Further in order to sustain the strong growth momentum, the management expects to diversify in other non ARV segments by tapping new therapy areas and new geographies. Also likely synergies from Laurus Bio provide ample visibility on growth going ahead. Strong topline growth and OPM expansion would lead to a sturdy 72% earnings CAGR over FY2020-FY2023. At CMP, the stock is trading at a valuation of 16.8x/14.2x 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 PT of Rs 410.

Key risk

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

Valuation (Consolidated)

Particulars	Rs cr				
	FY19	FY20	FY21E	FY22E	FY23E
Sales	2291.9	2831.7	4532.3	5395.9	6380.5
Operating Profits	356.0	564.5	1414.1	1662.0	1958.8
OPM(%)	15.5	19.9	31.2	30.8	30.7
PAT	93.8	255.3	920.7	1090.1	1294.5
PATM (%)	4.1	9.0	20.3	20.2	20.3
EPS	1.8	4.8	17.3	20.5	24.3
P/E	195.7	71.9	19.9	16.8	14.2
EV/EBIDTA	54.7	34.2	13.7	11.5	9.6
ROE (%)	6.0	14.4	34.2	28.8	25.5
ROCE (%)	7.2	13.2	32.2	29.6	27.8

Source: Company; Sharekhan estimates

Strong performance for the quarter: Laurus Labs reported yet another quarter of stellar performance. The earnings are ahead of ours as well as streets estimates by 17% as well as 10% respectively. Sales at Rs 1288.4 cr grew sturdily by 76.6% y-o-y and are ahead of estimates. The sturdy growth in revenues is on the back of a 104% y-o-y growth in the API segment revenues to Rs 731 crore, driven by a strong growth in the ARV API's. The generic FDF segment revenues were up 33% y-o-y to Rs 430 cr while the Synthesis segment revenues grew 10% y-o-y to Rs 127 cr. Operating profit grew sharply to Rs 425 crore as compared to 148 Cr in Q3FY20, up by 188% y-o-y and was ahead of estimates. The operating margins expanded by a stellar 1280 bps y-o-y to 33% and was ahead of the estimates. OPM expansion could be attributable to expansion of 420 bps y-o-y in gross margins, benefits of operating leverage and favourable mix. Tracking the strong operating performance, the PAT for the quarter stood at Rs 273 cr as compared to a Rs 73 cr in Q3FY20. The PAT was ahead of estimates

Strong demand traction, capacity expansion to fuel the topline growth: Laurus's revenues has staged another quarter of stellar performance with revenues growing by a stellar 76.7% y-o-y. The ARV API segment revenues have grown sturdily by 165% y-o-y led by higher growth in ARV. API business in turn led by higher volume of 1st line products. Laurus' formulations business too has staged a strong growth of 47% yoy on the back of a strong demand from the LMIC countries. The revenues from the formulations business has grown impressively to Rs. 430 crore from Rs. 292 crore in the corresponding quarter. The company's sees the tender business from the low and middle income countries (LMIC) to be 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, though has been delayed due to covid led challenges, it is now expected to be over by August 2021 while the second leg of expansion would be done in two phases and will be ready by FY2022. Cumulatively, the formulations capacity would increase by 80% over the next 2 years. Laurus is confident of revenues of around 1x from the said investments over years going ahead. Also, traction from the North America and EU is expected to sustain going ahead and would aid topline growth.

Diversification in to non ARV therapy areas, geographical expansion to drive growth over long term: Laurus is one of the leading players globally in the ARV space (both API and formulations). Going ahead in order to maintain the growth momentum the management is now evaluating building its presence in the non-ARV areas of anti-diabetology and cardiology. This would be achieved by tapping the new geographies of US and Europe and other markets. Further Laurus has filed / in the process of filing for few high market opportunity products in these space in the abovementioned markets. Also it expects to participate in certain tenders in the EU region which would enable it to grow its topline. However, the management sees this as a long term trigger and expects it to play out by FY2024-FY2025. However, we believe the diversification in other areas of diabetology and cardiology would enable the company to create new growth avenues and would augur well.

Key Conference call takeaways

- ♦ **Generic FDF:** Revenues from the segment continued its strong growth trajectory and grew by 47% y-o-y to Rs 430 crore. Growth in the quarter was led by higher sales from tender business in LMIC. The segment constituted 33% of the total quarterly sales. During the quarter, Laurus commenced marketing of in-licensed products in the US by leveraging its front end. Also the contract manufacturing revenues from the Europe region has a strong order book and which would support the growth beyond FY2021. Laurus has received final approvals for 9 products and 8 products have tentative approvals. Also the company has TLE400 in the RoW markets.
- ♦ **Europe – Contract Manufacturing opportunity:** Laurus has entered in to a long- term partnership with a leading generic player in Europe for Contract Manufacturing Opportunities. Under the agreement the partner would be responsible for marketing authorizations while Laurus would act as a contract manufacturer. Laurus sees the benefits from this arrangement to accrue post FY2023.

- ◆ **Generic API:** The segment sales grew by an impressive 103% y-o-y for the quarter, led by a strong 165% growth in the ARV API segment to Rs 568 crore. The oncology API and other API's grew by 36% and 1% y-o-y respectively.
- ◆ **Revenue Mix:** As of Q3FY2021, Laurus derives around 75% of its sales from the ARV segment (on an overall basis) which is primarily in them LMIC countries. While the balance 25% is from non ARV segment and is derived largely from the US and Europe. Going ahead, Laurus expects the share of Revenues from the non ARV segment to reach to 38% over the next 5 years as it sees to build / fortify its presence in the non ARV segment. The diversification in favor of non ARV segment bodes well for the company, though it is a long term driver. However over the next 1-2 years, Laurus sees traction in the Generic formulations segment to drive the growth.
- ◆ **Synthesis Business:** The Synthesis business segment revenues grew by 63% YoY for the quarter. As of the quarter the company has a total of 49 active projects in the segment nad has commercial supplies on going for 4 products.
- ◆ **ANDA filings:** Till date, laurus 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 282 patents, off which it has been granted 141 patents.
- ◆ **Laurus Bio:** Laurus has successfully completed the acquisition on Richcore LifeSciences and has renamed the company as Laurus Bio. It would be a CDMO company for recombinant proteins catering to food based as well as therapy based products. Laurus is also looking at exploring more synergies from the acquisition.

Results

Particulars	Rs cr				
	Q3FY2021	Q3FY2020	YoY %	Q2FY2021	QoQ %
Total Sales	1,288.4	729.6	76.6	1,138.8	13.1
Expenditure	862.7	581.9	48.2	765.5	12.7
Operating profit	425.8	147.7	188.3	373.3	14.0
Other income	6.9	1.9	260.2	5.1	35.4
EBITDA	432.7	149.6	189.2	378.4	14.3
Interest	17.4	20.8	-16.3	13.7	27.4
Depreciation	51.1	47.6	7.4	51.0	0.2
PBT	364.2	81.2	348.4	313.8	16.1
Taxes	91.3	8.2	1009.5	72.0	26.7
Adjusted PAT	272.9	73.0	273.9	241.7	12.9
Margins			BPS		BPS
OPM %	33.0	20.2	1,281	32.8	26

Source: Company; Sharekhan Research

Segment Revenues – Quarterly

Particulars	Rs cr				
	Q3FY2021	Q3FY2020	YoY %	Q2FY2021	QoQ %
ARV-API	568.0	214.0	165.4	379.0	49.9
Oncology-API	64.0	47.0	36.2	86.0	(25.6)
Other API	99.0	98.0	1.0	106.0	(6.6)
Synthesis	127.0	78.0	62.8	116.0	9.5
Generic FDF	430.0	292.1	47.2	452.0	(4.9)
Total	1,288.0	729.1	76.7	1,139.0	13.1

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.

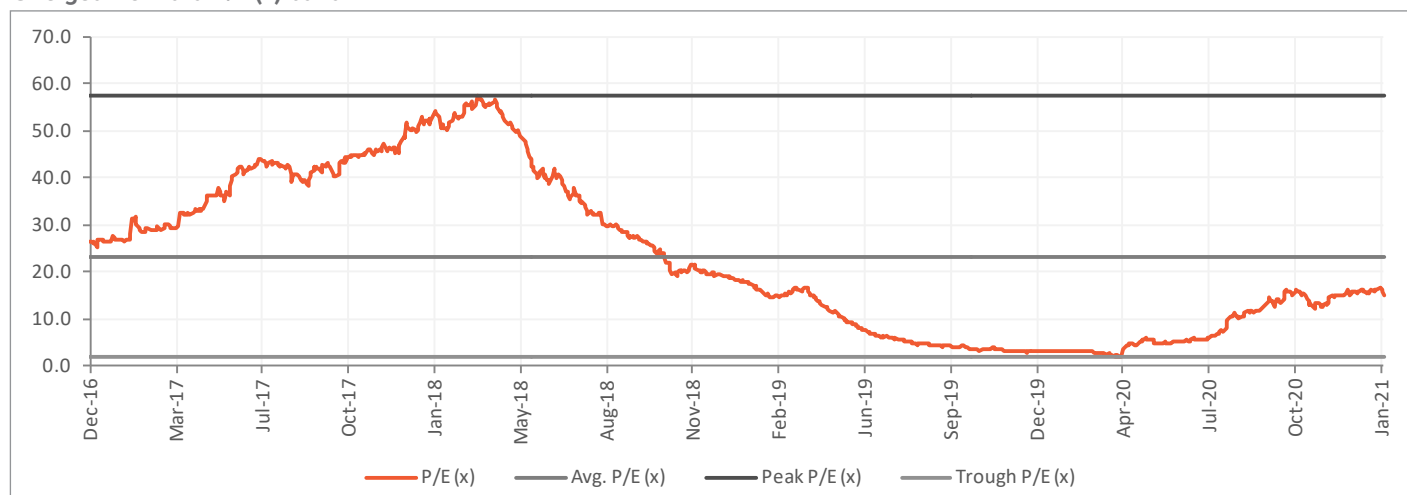
■ Company Outlook – Robust outlook

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 and management is confident of sustaining the strong growth momentum. Further over the long term Laurus looks to diversify in to other areas of Cardiology and diabetology and in the process reduce the dependence on the ARV segment. Also in the formulations segment the company has entered in to a contract manufacturing agreement with a partner in the EU region, which is expected to yield benefits over long term. Overall over the next 5 years the company expects the share of ARV in the total to come down to around 38% from a current level of 75%. Also synergies / new opportunities from Laurus Bio would also fuel the growth. Moreover, expected traction in the synthesis business would also be key revenue driver. Benefits of operating leverage and a favorable product mix would result in OPM expansion. Cumulatively, earnings are expected to grow by a 72% CAGR over FY2020-Fy2023.

■ Valuation – Retain Buy with PT of Rs 410

Q3FY2021 was yet another quarter of stellar performance. The strong growth trajectory is expected to sustain going ahead as well. The formulations business is well placed to harness the opportunities and the management is confident of sustaining the momentum going ahead. Further, Laurus is increasing its formulation capacity to cater to the surging demand. 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. Further in order to sustain the strong growth momentum, the management expects to diversify in other non ARV segments by tapping new therapy areas and new geographies. Also likely synergies from Laurus Bio provide ample visibility on growth going ahead. Strong topline growth and OPM expansion would lead to a sturdy 72% earnings CAGR over FY2020-FY2023. At CMP, the stock is trading at a valuation of 16.8x/14.2x 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 PT of Rs 410

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	345.0	53.2	18,087.0	19.9	16.8	13.7	11.5	34.2	28.8
Lupin	1008	45.3	49,063	42.2	24.8	16.5	11.3	8.0	11.9
Aurobindo	998	58.6	58476	16.9	14.7	10.2	8.4	17.2	16.8

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 its 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. Moreover, the company is doubling its capacity to support growth in the formulations business, which points towards healthy growth going ahead. The recent acquisition of RLPL by Laurus marks its entry into the lucrative biologics space and would be growth accretive over the medium to long term.

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 Website

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

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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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