

Alkem Labs

Looking beyond near term margin weakness

Result Synopsis

Alkem margin came in lower than estimate on higher input costs (gross margin had one off in base quarter) and steep price erosion in US. PAT was suppressed due to additional tax provision arising from a court judgement coupled with Rs150mn investment write off in US business.

Alkem guided to gross margin pressure especially in the busy H1 FY23 – we reckon a tug of war between price hikes in NLEM/non NLEM portfolio and liquidation of high cost inventory purchased in 4Q and could last till end of H1. US business showed a 5% decline in FY22 on back of sharp price erosion in high mid-teens – a factor which could moderate in current fiscal as companies respond quicker with product rationalization (our expectation) as also commentary from generics giant Sandoz (expects bottoming out of US business and back to growth per 1Q CY22 call). While we have factored growth in line with US guidance, there could be room for surprise if price erosion moderates sharply. Margin performance in domestic business would be in focus compared to growth in H1 FY23. We cut our FY23 margin estimate by ~200bps resulting in a ~7% EPS cut though gross margin to revert to 61% in FY24 translating in to margin recovery at 20%. Our BUY stays based on unchanged 23x with marginally revised TP Rs3,900 (earlier Rs3,950); near term margin uncertainty does not dilute our positive view on the stock.

Result Highlights

- Revenue up 13.3% YoY to Rs 24,839mn, higher than our estimate of 12% growth YoY.
- India business grew ahead of IPM delivering 16.7% growth for the quarter YoY. Anti-infectives, pain and respiratory delivered double digit growth rates.
- US sales were flat due to high price erosion in base portfolio. Other International markets continued strong performance delivering 34.8% growth YoY in Q4FY22.
- Operating margins came in at 13.6% and were flat on YoY basis but fell ~550bps sequentially as high RM prices affected the margins.
- PAT was lower due to higher tax adjustment for previous periods and one time adjustment on fair value of one of its US investments. (Rs150mn)
- Management alludes to inflationary pressures of high RM prices & increased freight costs being a key challenge.

Exhibit 1: Actual vs estimates

Rs Mn	Actual	Estimates		% Variation		Remarks
		Yes Sec	Consensus	YES Sec	Consensus	
Sales	24,839	24,650	24,452	0.8	1.6	Margin miss on steep price erosion & higher COGS
EBITDA	3,372	3,600	3,979	(6.3)	(15.2)	
OPM (%)	13.6	14.6	16.3	-103bps	-270bps	
Adjusted PAT	1,232	2,816	2,951	(56.3)	(58.3)	

Source: Company, YES Sec

Reco : **BUY**

CMP : Rs 2903

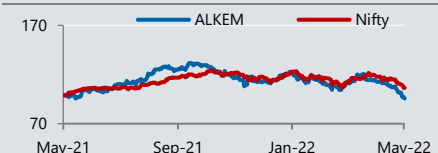
Target Price : Rs 3900

Potential Return : 34%

Stock data (as on May 13, 2022)

Nifty	15,782
52 Week h/l (Rs)	4070 / 2832
Market cap (Rs/USD mn)	347426 / 4486
Outstanding Shares (mn)	120
6m Avg t/o (Rs mn):	394
Div yield (%):	1.2
Bloomberg code:	ALKEM IN
NSE code:	ALKEM

Stock performance



	1M	3M	1Y
Absolute return	-15.0%	-15.3%	-2.3%

Shareholding pattern (As of Mar'22 end)

Promoter	57.1%
FII+DII	19.3%
Others	23.5%

Δ in stance

(1-Yr)	New	Old
Rating	BUY	BUY
Target Price	3900	3950

Δ in earnings estimates

	FY23e	FY24e
EPS (New)	134.4	168.6
EPS (Old)	144.3	171.4
% change	-6.9	-1.6

Financial Summary

(Rs mn)	FY22	FY23E	FY24E
Revenue	106,342	116,099	128,231
YoY Growth	20.0	9.2	10.4
EBITDA	20,529	20,971	25,768
YoY Growth	5.7	2.2	22.9
PAT	16,456	16,065	20,159
YoY Growth	3.8	(2.4)	25.5
ROE	21.2	17.4	19.0
EPS	137.6	134.4	168.6
P/E	21.1	21.6	17.2
BV	722.5	821.8	955.3
EV/EBITDA	15.8	15.7	12.4

BHAVESH GANDHI

Lead Analyst

bhavesh.gandhi@ysil.in

+91 22 6885 0521

YASH SINGHEE, Associate

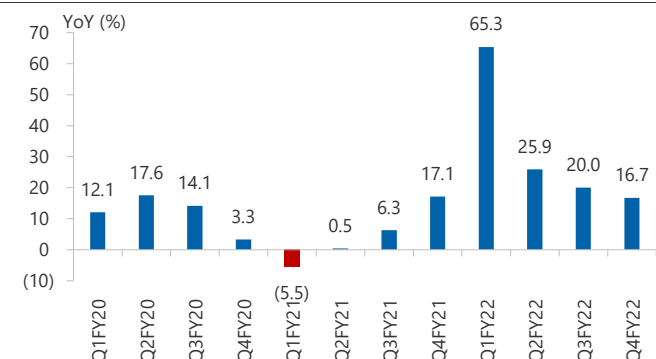


Exhibit 2: Quarterly snapshot

Rs mn	Q4 FY21	Q1 FY22	Q2 FY22	Q3 FY22	Q4 FY22	y/y (%)	q/q (%)	FY22	FY21	y/y (%)
Revenue	21,922	27,314	28,000	26,190	24,839	13.3	(5.2)	106,342	88,650	20.0
Expenditure	19,011	21,385	21,756	21,205	21,466	12.9	1.2	85,813	69,226	24.0
- RM	9,430	10,948	10,575	9,967	10,314	9.4	3.5	41,803	34,985	19.5
Gross Profit	12,492	16,366	17,425	16,223	14,525	16.3	(10.5)	64,539	53,666	20.3
GM(%)	57.0	59.9	62.2	61.9	58.5	149 bps	-347 bps	60.7	60.5	15 bps
- Staff Cost	4,090	5,318	4,945	4,709	4,655	13.8	(1.1)	19,627	16,210	21.1
- Other Cost	5,490	5,119	6,237	6,530	6,498	18.4	(0.5)	24,383	18,031	35.2
Operating Profit	2,911	5,929	6,244	4,985	3,372	15.8	(32.3)	20,529	19,424	5.7
OPM(%)	13.3	21.7	22.3	19.0	13.6	30 bps	-546 bps	19.3	21.9	-261 bps
Other Income	463	467	420	535	205	(56)	(62)	1,627	2,332	(30.3)
Depreciation	685	705	728	775	831	21	7	3,040	2,746	10.7
Interest	107	129	120	106	170	58	61	524	589	(11.1)
PBT	2,582	5,561	5,816	4,639	2,576	(0.2)	(44.5)	18,592	18,421	0.9
Tax	89	759	230	(694)	1,345	1,404.1	(293.7)	1,640	2,243	(26.9)
PAT	2,492	4,802	5,586	5,334	1,232	(50.6)	(76.9)	16,953	16,178	4.8
Exceptional Loss/(Profit)	-	-	-	-	150	-	-	150	-	
Reported PAT	2,492	4,802	5,586	5,334	1,082	(56.6)	(79.7)	16,803	16,178	3.9
Adjusted PAT	2,492	4,802	5,586	5,334	1,232	(50.6)	(76.9)	16,953	16,178	4.8

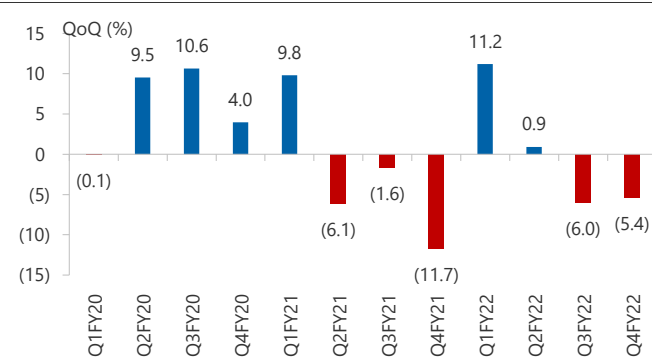
Source: Company, YES Sec

Exhibit 3: India business outperforms IPM



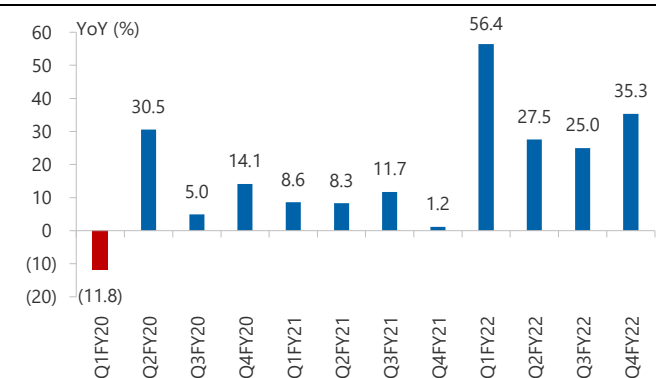
Source: Company, YES Sec

Exhibit 4: US impacted by price erosion



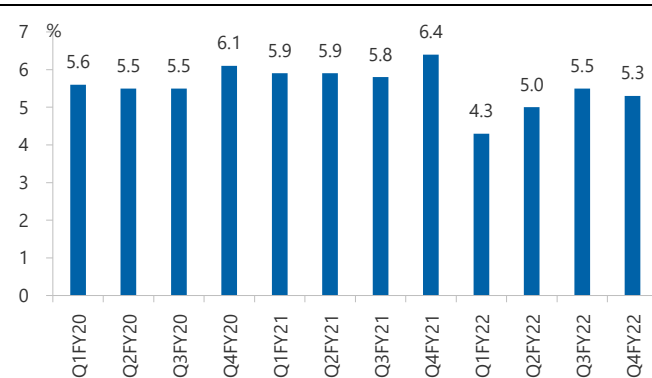
Source: Company, YES Sec

Exhibit 5: ROW continues to deliver strong growth



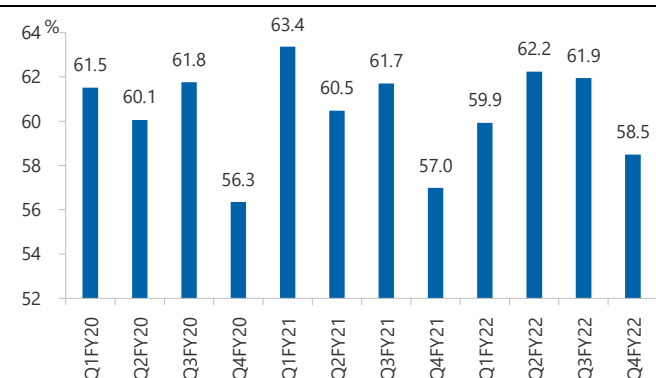
Source: Company, YES Sec

Exhibit 6: R&D spending % of sales



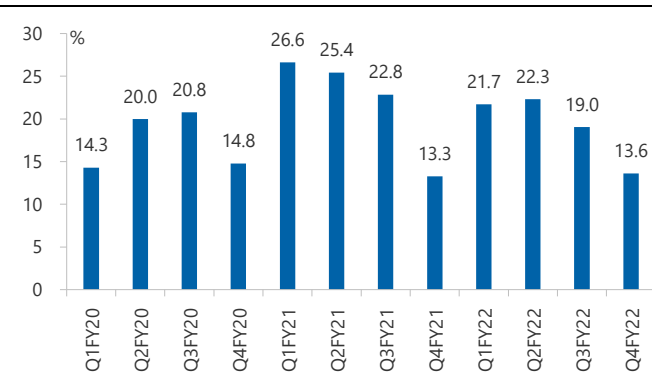
Source: Company, YES Sec

Exhibit 7: High RM costs impact gross margins



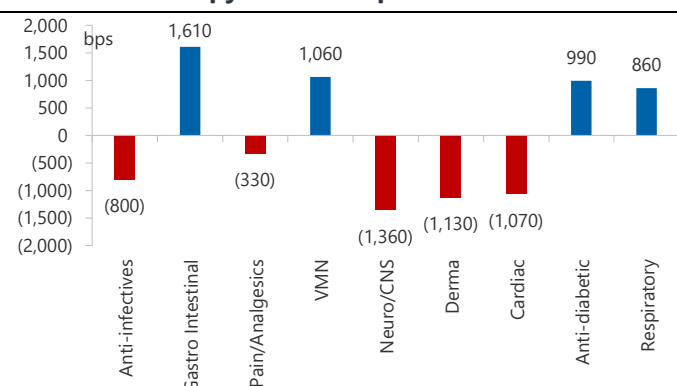
Source: Company, YES Sec

Exhibit 8: Operating margins also show a dip



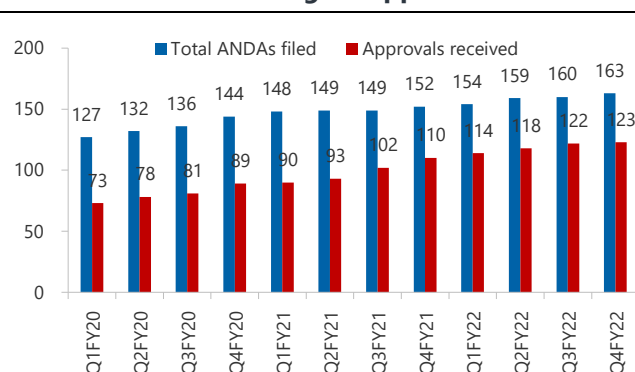
Source: Company, YES Sec

Exhibit 9: Therapy wise – Outperformance Vs IPM



Source: Company, YES Sec

Exhibit 10: ANDAs – filings & approvals



Source: Company, YES Sec

KEY CON-CALL HIGHLIGHTS

US

- Currently sell 85 ANDAs in US out of which 15 may not have reached potential due to lack of competitiveness from Alkem or newly launched products.
- Not slipped back into the red in US even at PBT level.
- NRV got impacted by 1.6-1.7% due to price erosion and similar is impact of higher RM cost.
- Full year price erosion was 11-12%, expecting it be in high single digits going forward.
- Margins have remained steady in the US business since last few quarters.
- On diabetes front, really strong pipeline and some can be blockbusters helping to reach 20bn in next 4 years.

India

- 22% is trade generics and out of 78%, 85% is acute and 15% is chronic.
- Will continue to deliver double digit growth on a strong base of last year.
- Price increases would be higher (~7%) along with 3-5% volume growth in FY23.
- Not focusing on any therapy in trade generics, just getting the help of Alkem brand name to sell majorly acute and some chronic drugs.
- 10000 MRs, out of which 19% in chronic and rest in acute.
- Alkem has a very strong business in Trade generics despite lots of competitors entering.
- Growth in acute should be 10-11% in FY23 and chronic should grow twice the market around 20%. Trade generics has usually seen higher growth and should continue to do so.
- International Markets
- Similar markets being catered for few years now. New launches were high with low level of price erosion has helped to deliver good growth.
- Double digit growth will sustain in these markets.

Enzene

- 3 product launches in India and several CDMO projects started this year.

Margins

- Material prices have started softening but whatever material already has been procured has to be used and may affect some margins in Q1.
- Freight charges can see upticks further and can have impact on margins.
- 150-170bps impact on Gross margins further can be seen in Q1 and Q2 of FY23 in comparison to last year basis (YoY basis).
- All price increases done this year weren't able to compensate to hike in RM prices.

Guidance

- No large acquisition plans.
- Will guide for 18% margins in FY23 and will try to improve it next year onwards.

Alkem Labs

- Lower double-digit revenue growth (10-12%) is what the company is guiding for US over the next few years.
- India and US will see capex, with biosimilar seeing major capex out of it. No other large capex planned in the next 1-2 years.
- Tax rate is expected to be 11-14% in the next 1-2 years.
- Biosimilars: 1bn investment for next 1-2 years on operations. Currently contributing huge losses. This investment can go up after a couple of years.
- No step up in MR addition. Already done for growing large and medium sized brands.

FINANCIALS

Exhibit 11: Balance Sheet

Y/e 31 Mar (Rs m)	FY20	FY21	FY22	FY23E	FY24E
Equity capital	239	239	239	239	239
Reserves	61,367	73,528	86,140	98,008	113,971
Net worth	61,606	73,767	86,379	98,247	114,210
MI	1,480	1,813	2,094	2,094	2,094
Debt	3,908	3,572	4,165	4,165	4,165
Def.tax lia	3	0	0	0	0
Total liabilities	66,997	79,152	92,639	104,507	120,469
Fixed assets	32,713	31,857	32,411	34,411	36,411
Investments	2,442	2,963	10,833	10,833	10,833
Net working capital	22,517	33,254	36,302	46,171	60,133
Inventories	18,188	23,124	30,055	32,813	36,242
Sundry debtors	16,493	16,072	18,846	20,575	22,725
Cash	12,611	21,699	27,179	21,953	31,675
Other current assets	7,657	8,399	8,274	10,449	11,541
Sundry creditors	(9,540)	(10,694)	(11,734)	(12,810)	(14,149)
Other current liabilities	(22,892)	(25,346)	(36,319)	(26,809)	(27,900)
Def tax assets	9,325	11,079	13,092	13,092	13,092
Total assets	66,997	79,152	92,639	104,507	120,469

Source: Company, YES Sec

Exhibit 12: Income statement

Y/e 31 Mar (Rs m)	FY20	FY21	FY22	FY23E	FY24E
Revenue	83,443	88,650	106,342	116,099	128,231
Operating profit	14,734	19,424	20,529	20,971	25,768
Depreciation	(2,527)	(2,746)	(3,040)	(3,203)	(3,563)
Interest expense	(651)	(589)	(524)	(1,139)	(924)
Other income	1,040	2,332	1,626	1,626	1,626
Profit before tax	12,596	18,421	18,592	18,255	22,908
Taxes	(1,104)	(2,243)	(1,640)	(2,191)	(2,749)
Adj. profit	11,492	16,178	16,952	16,065	20,159
Exceptional item	(222)	(328)	(497)	-	-
Net profit	11,270	15,850	16,456	16,065	20,159

Source: Company, YES Sec

Exhibit 13: Growth and Ratio matrix

Y/e 31 Mar	FY20	FY21	FY22	FY23E	FY24E
Growth matrix (%)					
Revenue growth	13.4	6.2	20.0	9.2	10.4
Op profit growth	32.2	31.8	5.7	2.2	22.9
EBIT growth	31.3	43.5	0.6	1.5	22.9
Net profit growth	48.2	40.6	3.8	(2.4)	25.5

Profitability ratios (%)

OPM	17.7	21.9	19.3	18.1	20.1
EBIT margin	15.9	21.4	18.0	16.7	18.6
Net profit margin	13.8	18.2	15.9	13.8	15.7
RoCE	20.8	26.0	22.3	19.7	21.2
RoNW	19.8	23.9	21.2	17.4	19.0
RoA	13.9	16.7	14.6	12.4	14.4

Per share ratios

EPS	94.3	132.6	137.6	134.4	168.6
Dividend per share	25.0	30.0	30.0	30.0	30.0
Cash EPS	117.3	158.3	167.2	161.2	198.4
Book value per share	515.3	617.0	722.5	821.8	955.3

Valuation ratios (x)

P/E	30.8	21.9	21.1	21.6	17.2
P/BV	5.6	4.7	4.0	3.5	3.0
M Cap/Sales	4.2	3.9	3.3	3.0	2.7
EV/EBIDTA	23.0	16.9	15.8	15.7	12.4

Payout (%)

Tax payout	8.8	12.2	8.8	12.0	12.0
Dividend payout	31.0	26.5	28.9	26.1	20.8

Liquidity ratios

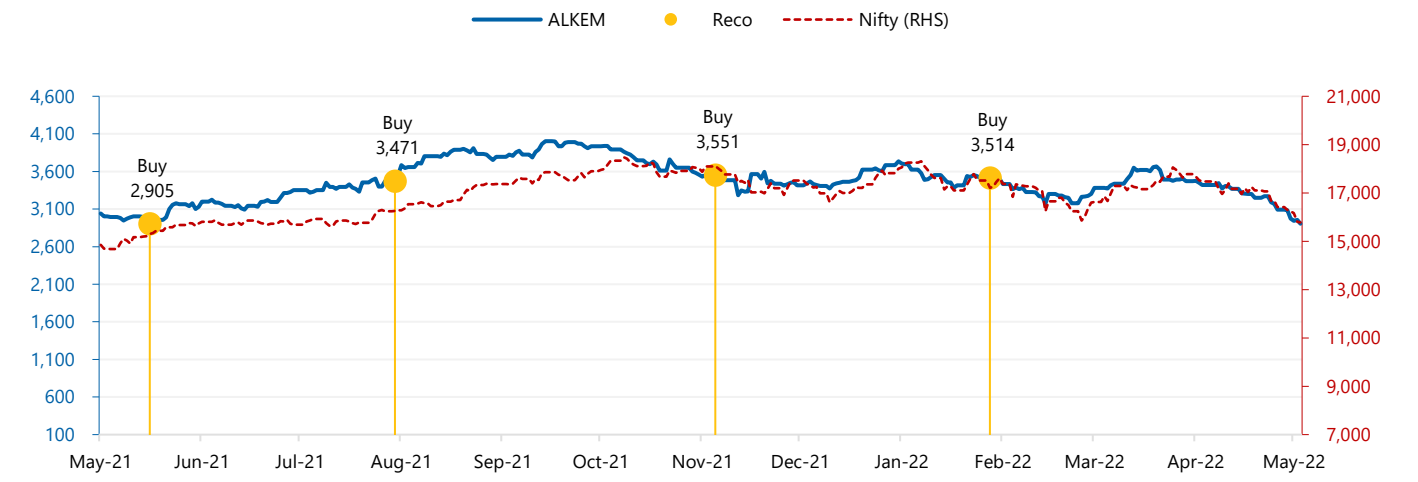
Debtor days	72	66	65	65	65
Inventory days	80	95	103	103	103
Creditor days	42	44	40	40	40

Leverage ratios

Interest coverage	20.4	32.3	36.5	17.0	25.8
Net debt / equity	(0.1)	(0.2)	(0.3)	(0.2)	(0.2)
Net debt / op. profit	(0.6)	(0.9)	(1.1)	(0.8)	(1.1)

Source: Company, YES Sec

Recommendation Tracker



DISCLAIMER

Investments in securities market are subject to market risks, read all the related documents carefully before investing.

The information and opinions in this report have been prepared by YSL and are subject to change without any notice. The report and information contained herein are strictly confidential and meant solely for the intended recipient and may not be altered in any way, transmitted to, copied or redistributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of YSL.

The information and opinions contained in the research report have been compiled or arrived at from sources believed to be reliable and have not been independently verified and no guarantee, representation of warranty, express or implied, is made as to their accuracy, completeness, authenticity or validity. No information or opinions expressed constitute an offer, or an invitation to make an offer, to buy or sell any securities or any derivative instruments related to such securities. Investments in securities are subject to market risk. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. Investors should note that each security's price or value may rise or fall and, accordingly, investors may even receive amounts which are less than originally invested. The investor is advised to take into consideration all risk factors including their own financial condition, suitability to risk return profile and the like, and take independent professional and/or tax advice before investing. Opinions expressed are our current opinions as of the date appearing on this report. Investor should understand that statements regarding future prospects may not materialize and are of general nature which may not be specifically suitable to any particular investor. Past performance may not necessarily be an indicator of future performance. Actual results may differ materially from those set forth in projections.

Technical Analysis reports focus on studying the price movement and trading turnover charts of securities or its derivatives, as opposed to focussing on a company's fundamentals and opinions, as such, may not match with reports published on a company's fundamentals.

YSL, its research analysts, directors, officers, employees and associates accept no liabilities for any loss or damage of any kind arising out of the use of this report. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject YSL and associates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

YES Securities (India) Limited (YSL) distributes research and engages in other approved or allowable activities with respect to U.S. Institutional Investors through SEC 15a-6 rules and regulations under an exclusive chaperone arrangement with Brasil Plural Securities LLC. The views and sentiments expressed in this research report and any findings thereof accurately reflect YSL analyst's truthful views about the subject securities and or issuers discussed herein. YSL is not registered as a broker-dealer under the Securities Exchange Act of 1934, as amended (the "Exchange Act") and is not a member of the Securities Investor Protection Corporation ("SIPC"). Brasil Plural Securities LLC is registered as a broker-dealer under the Exchange Act and is a member of SIPC. For questions or additional information, please contact Gil Aikins (gil.aikins@brasilplural.com) or call +1 212 388 5600.

DISCLOSURE OF INTEREST

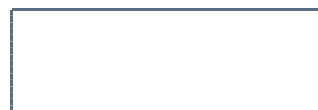
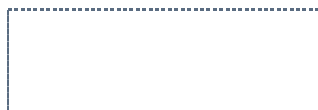
Name of the Research Analyst : Bhavesh Gandhi, Yash Singhee

The analyst hereby certifies that opinion expressed in this research report accurately reflect his or her personal opinion about the subject securities and no part of his or her compensation was, is or will be directly or indirectly related to the specific recommendation and opinion expressed in this research report.

Sr. No.	Particulars	Yes/No
1	Research Analyst or his/her relative's or YSL's financial interest in the subject company(ies)	No
2	Research Analyst or his/her relative or YSL's actual/beneficial ownership of 1% or more securities of the subject company(ies) at the end of the month immediately preceding the date of publication of the Research Report	No
3	Research Analyst or his/her relative or YSL has any other material conflict of interest at the time of publication of the Research Report	No
4	Research Analyst has served as an officer, director or employee of the subject company(ies)	No
5	YSL has received any compensation from the subject company in the past twelve months	No
6	YSL has received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
7	YSL has received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months	No
8	YSL has received any compensation or other benefits from the subject company or third party in connection with the research report	No
9	YSL has managed or co-managed public offering of securities for the subject company in the past twelve months	No
10	Research Analyst or YSL has been engaged in market making activity for the subject company(ies)	No

Since YSL and its associates are engaged in various businesses in the financial services industry, they may have financial interest or may have received compensation for investment banking or merchant banking or brokerage services or for any other product or services of whatsoever nature from the subject company(ies) in the past twelve months or associates of YSL may have managed or co-managed public offering of securities in the past twelve months of the subject company(ies) whose securities are discussed herein.

Associates of YSL may have actual/beneficial ownership of 1% or more and/or other material conflict of interest in the securities discussed herein.



YES Securities (India) Limited

Registration Nos.: CIN: U74992MH2013PLC240971 | SEBI Single
Registration No.: NSE, BSE, MCX & NCDEX: INZ000185632 | Member Code:
BSE – 6538, NSE – 14914, MCX – 56355 & NCDEX - 1289 | MERCHANT
BANKER: INM000012227 | RESEARCH ANALYST: INH000002376 |
INVESTMENT ADVISER: INA000007331 | Sponsor and Investment Manager

Registered Address: 2nd Floor, North Side, YES BANK House,
Off Western Express Highway, Santacruz East,
Mumbai - 400 055, Maharashtra, India.

Correspondence Address: 4th Floor, AFL House,
Lok Bharti Complex, Marol Maroshi Road, Andheri East,
Mumbai - 400059, Maharashtra, India.

☎ +91 22 68850521 | ✉ research@ysil.in
Website: www.yesinvest.in

to YSL Alternates Alpha Plus Fund (Cat III AIF) SEBI Registration No.:
IN/AIF3/20-21/0818 | AMFI ARN Code – 94338.

Details of Compliance Officer: Name: Vaibhav Purohit,
Email id: compliance@ysil.in, Contact No: +91-22-6885 0278