

Industry Pharmaceuticals  
Bloomberg ALKEM IN  
BSE CODE 539523

## Growth across geographies, lower tax rate drives profitability.

| RATING           | NEUTRAL |
|------------------|---------|
| CMP              | 2506    |
| Price Target     | 2536    |
| Potential Upside | 1%      |

|                 |   |
|-----------------|---|
| Rating Change   | ↓ |
| Estimate Change | ↑ |
| Target Change   | ↑ |

| STOCK INFO          |           |
|---------------------|-----------|
| 52wk Range H/L      | 2699/1660 |
| Mkt Capital (Rs Cr) | 31589     |
| Free float (%)      | 34%       |
| Avg. Vol 1M (,000)  | 114       |
| No. of Shares (Crs) | 12        |
| Promoters Pledged % | 0%        |

### 3QFY20 Result Update

- Overall sales grew by 13% YoY to Rs. 2182 crs (vs our estimate of Rs.2161) during the quarter majorly on account of growth across geographies.
- India business grew 14.1% YoY to Rs. 1424 crs, Acute and chronic segments grew by 13% and 21% YoY respectively.
- The US business grew by 15% YoY to US\$ 83 mn on account of volume traction and new launches, expects lower double digit growth going ahead.
- Gross margin increased by 450 bps YoY to 61.8% this quarter on account of product mix and softening of API prices. EBITDA margin grew by 483 bps YoY to 20.8%.
- PAT grew by 90% YoY to Rs. 390 crs on account of the lower tax rate. PAT margin for the quarter stood at 17.9%.

### View and Valuation

ALKEM reported decent growth of 13% this quarter majorly on account of growth across geographies. The India and US business grew strongly by 14% and 15% respectively. The softening of the API prices and product mix led to margin expansion. PAT grew strongly by 90% YoY to Rs. 390 crs due to the lower tax rates.

Going ahead, the company has strategized well to grow across the markets in order to drive the profitability. In the India business, the major focus of the company would be to grow its semi-chronic and chronic segments where the margins are high. In the US market, the company plans to file 12-15 products, and launch lower double digit products every year going forward. Based on lower tax rate for the company, we have increased our PAT estimate for FY20 and FY21 by 15% and 9% respectively. Therefore, we value the stock at 24x FY21E EPS to arrive at a target price of Rs 2536 and maintain NEUTRAL.

### Key Risks to our rating and target

- R&D spends to 5-6% of sales.
- 3 483s in St. Louis facility.

### RESEARCH ANALYST

**J MADHAVI**

j.madhavi@narnolia.com

Fig in Rs Cr

| KEY FINANCIAL/VALUATIONS | FY17 | FY18 | FY19 | FY20E | FY21E |
|--------------------------|------|------|------|-------|-------|
| Net Sales                | 5853 | 6431 | 7357 | 8422  | 9443  |
| EBITDA                   | 999  | 1028 | 1115 | 1540  | 1604  |
| EBIT                     | 898  | 885  | 922  | 1309  | 1360  |
| PAT                      | 892  | 631  | 774  | 1251  | 1264  |
| EPS (Rs)                 | 75   | 53   | 65   | 105   | 106   |
| EPS growth (%)           | 20%  | -29% | 23%  | 62%   | 1%    |
| ROE (%)                  | 20%  | 13%  | 14%  | 19%   | 17%   |
| ROCE (%)                 | 19%  | 18%  | 16%  | 19%   | 18%   |
| BV                       | 374  | 407  | 455  | 544   | 631   |
| P/B (X)                  | 5.9  | 4.9  | 3.9  | 4.6   | 4.0   |
| P/E (x)                  | 29.6 | 37.5 | 27.1 | 23.9  | 23.7  |

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## 3QFY20 Results

Fig in Rs Cr

| FINANCIALS       | 3QFY19 | 4QFY19 | 1QFY20 | 2QFY20 | 3QFY20 | YoY %  | QoQ%   | FY18  | FY19  | YoY % |
|------------------|--------|--------|--------|--------|--------|--------|--------|-------|-------|-------|
| Net Sales        | 1,925  | 1,854  | 1,850  | 2,264  | 2,182  | 13.3%  | -3.6%  | 6,431 | 7,357 | 14.4% |
| Other Income     | 9      | 28     | 17     | 31     | 28     | 209.6% | -11.3% | 96    | 88    | -8.6% |
| COGS             | 823    | 776    | 712    | 904    | 834    | 1.4%   | -7.7%  | 2,513 | 2,945 | 17.2% |
| Gross Margin     | 57%    | 58%    | 62%    | 60%    | 62%    | 4.5%   | 1.7%   | 61%   | 60%   | -1.0% |
| Employee Cost    | 346    | 349    | 390    | 390    | 396    | 14.2%  | 1.5%   | 1,192 | 1,362 | 14.3% |
| Other Expen.     | 444    | 495    | 483    | 518    | 499    | 12.3%  | -3.7%  | 1,698 | 1,935 | 13.9% |
| EBITDA           | 312    | 235    | 265    | 453    | 453    | 45.4%  | 0.2%   | 1,028 | 1,115 | 8.4%  |
| EBITDA Mar.      | 16%    | 13%    | 14%    | 20%    | 21%    | 4.6%   | 0.8%   | 16%   | 15%   | -0.8% |
| Depreciation     | 48     | 57     | 56     | 56     | 59     | 24.7%  | 5.5%   | 143   | 193   | 35.1% |
| EBIT             | 264    | 178    | 209    | 396    | 394    | 49%    | -0.6%  | 885   | 922   | 4.1%  |
| Interest         | 15     | 7      | 16     | 18     | 17     | 11%    | -4.0%  | 55    | 55    | -1.3% |
| PBT              | 258    | 199    | 210    | 410    | 405    | 56.8%  | -1.3%  | 926   | 955   | 3%    |
| Exceptional Item | -      | -      | -      | -      | -      |        |        | -     | -     |       |
| Tax              | 53     | 28     | 23     | 29     | 15     | -72.2% | -50.1% | 288   | 181   | -37%  |
| PAT              | 205    | 171    | 187    | 380    | 390    | 89.8%  | 2%     | 638   | 774   | 21%   |
| PAT Margin       | 11%    | 9%     | 10%    | 17%    | 18%    | 7.2%   | 1%     | 10%   | 11%   | 1%    |

## Concall Highlights

- Revenue from operation grew by 13% YoY to Rs. 2182 crs. India business grew 14.1% YoY to Rs. 1424 crs and US business grew by 13% YoY to Rs. 584 crs.
- In the India business, Acute and chronic segments grew by 13% and 21% YoY respectively.
- The US business grew by 13% YoY on account of volume traction and new launches, expects lower double digit growth going ahead.
- Gross margin increased by 450 bps YoY to 61.8% this quarter on account of product mix and softening of API prices.
- The company filed 4 ANDAs and received approval for 4 ANDAs. For the 9MFY20, the company filed 11 ANDAs and 15 approvals.
- Of the cumulative 135 ANDAs filed, 70 received final approvals- of which 80% has been commercialized.
- In the India Business, the acute, semi-chronic and chronic contributes equally. The strategy going ahead would be to grow semi-chronic and chronic therapy.
- The strategy for the India business would be:
  - To grow the Chronic and semi-chronic segment which contributes in the range of 10-20 crs – to identify 1-2 division which can be in the range of 50-100 crs in the next 3-4 yrs.
  - Intends to grow the bigger division having the brand range of 20-50 crs.
- In the US market, the company plans to file 12-15 products, and launch lower double digit products every year going ahead.
- On the regulatory front, St.Louis facility in US received 3 483s for the inspection conducted from 27 Jan -6 Feb 2020.
- R&D for the quarter stood at Rs. 122 crs (5.5% of sales), the company expects the R&D cost to be 6% of sales in FY21 and FY22. The free cash flow for 9MFY20 stood at Rs.100 crs.
- Capex for 9MFY20 stands at Rs.300 crs, the company expects to end the year in the range of Rs.400-450 crs. In FY21, the capex is expected to be in the range of Rs. 350-400 crs.
- Short to medium term EBITDA margin expected to be in the range 20%.
- ETR for FY20- 10%.

## Operational Details

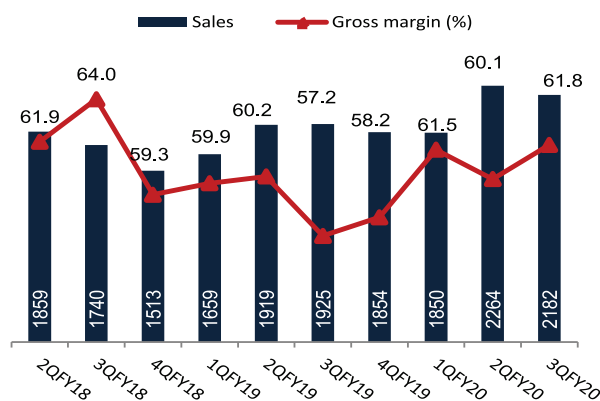
| GEOGRAPHY                   | 2QFY18 | 3QFY18 | 4QFY18 | 1QFY19 | 2QFY19 | 3QFY19 | 4QFY19 | 1QFY20 | 2QFY20 | 3QFY20 |
|-----------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Domestic                    | 1406   | 1257   | 960    | 1091   | 1318   | 1248   | 1218   | 1222   | 1550   | 1424   |
| US                          | 304    | 359    | 407    | 424    | 473    | 518    | 482    | 482    | 528    | 584    |
| Other International markets | 134    | 107    | 117    | 124    | 108    | 135    | 128    | 109    | 142    | 142    |

| REVENUE GR. %               | 2QFY18 | 3QFY18 | 4QFY18 | 1QFY19 | 2QFY19 | 3QFY19 | 4QFY19 | 1QFY20 | 2QFY20 | 3QFY20 |
|-----------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Domestic                    | 15%    | 22%    | 12%    | 26%    | -6%    | -1%    | 27%    | 12%    | 18%    | 14%    |
| US                          | 1%     | 6%     | 40%    | 43%    | 55%    | 44%    | 18%    | 14%    | 12%    | 13%    |
| Other International markets | 54%    | 14%    | 23%    | 13%    | -19%   | 26%    | 9%     | -12%   | 31%    | 5%     |

| Revenue Mix                 | 2QFY18 | 3QFY18 | 4QFY18 | 1QFY19 | 2QFY19 | 3QFY19 | 4QFY19 | 1QFY20 | 2QFY20 | 3QFY20 |
|-----------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Domestic                    | 76%    | 72%    | 63%    | 66%    | 69%    | 65%    | 66%    | 66%    | 68%    | 65%    |
| US                          | 16%    | 21%    | 27%    | 26%    | 25%    | 27%    | 26%    | 26%    | 23%    | 27%    |
| Other International markets | 7%     | 6%     | 8%     | 7%     | 6%     | 7%     | 7%     | 6%     | 6%     | 6%     |
| Others                      | 1%     | 1%     | 2%     | 1%     | 1%     | 1%     | 1%     | 2%     | 2%     | 2%     |

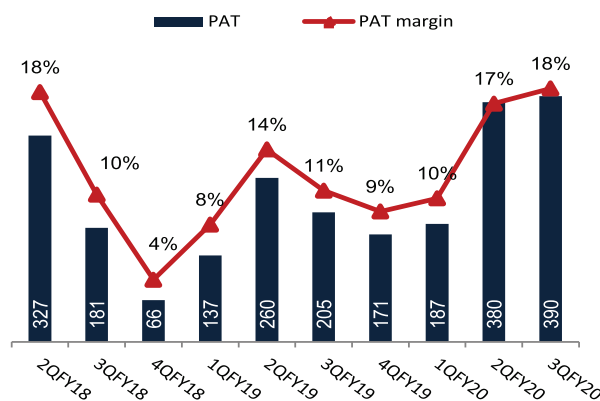
### Exhibit: Sales and Sales growth

Overall sales grew by 13% YoY to Rs. 2182 crs (vs our estimate of Rs.2161) during the quarter.



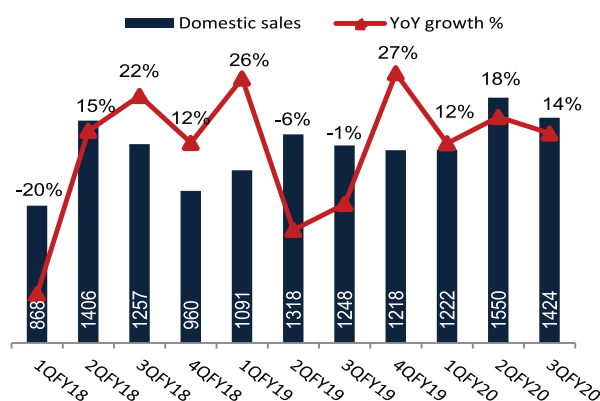
### Exhibit: PAT and PAT Margin

PAT grew by 90% YoY to Rs. 390 crs on account of the lower tax rate. PAT margin stood at 17.9%.



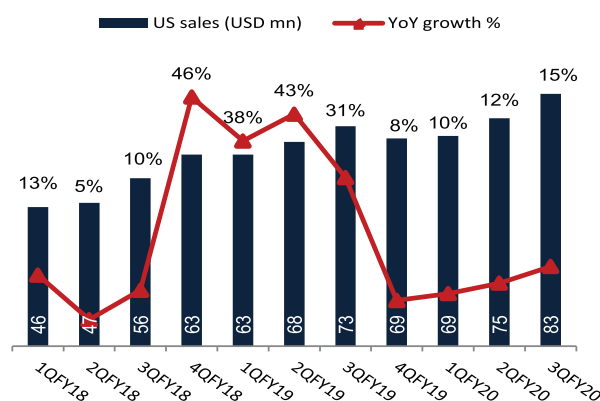
### Exhibit: Domestic sales and YoY growth

India business grew 14.1% YoY, acute and chronic segments grew by 13% and 21% YoY respectively.



### Exhibit: PAT and PAT Margin

The US business grew by 15% YoY to US\$ 83 mn on account of volume traction and new launches.



## Financial Details

### Balance Sheet

Fig in Rs Cr

| Y/E March                     | FY14         | FY15         | FY16         | FY17         | FY18         | FY19         | FY20E        | FY21E         |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|---------------|
| Share Capital                 | 12           | 24           | 24           | 24           | 24           | 24           | 24           | 24            |
| Reserves                      | 2,643        | 2,975        | 3,668        | 4,444        | 4,840        | 5,415        | 6,476        | 7,524         |
| <b>Networth</b>               | -            | -            | -            | -            | -            | -            | -            | -             |
| Debt                          | 1,077        | 1,248        | 683          | 769          | 1,014        | 1,035        | 1,275        | 947           |
| Other Non Current Liab        | 96           | 172          | 87           | 114          | 166          | 215          | 246          | 273           |
| <b>Total Capital Employed</b> | <b>2,875</b> | <b>3,009</b> | <b>3,792</b> | <b>4,625</b> | <b>4,971</b> | <b>5,647</b> | <b>6,810</b> | <b>7,730</b>  |
| Net Fixed Assets (incl CWIP)  | 980          | 1,143        | 1,269        | 1,751        | 2,319        | 2,666        | 3,010        | 3,190         |
| Non Current Investments       | 338          | 420          | 234          | 259          | 196          | 96           | 150          | 150           |
| Other Non Current Assets      | 1,417        | 1,395        | 1,263        | 1,640        | 1,235        | 1,230        | 1,348        | 1,365         |
| <b>Non Current Assets</b>     | <b>2,735</b> | <b>2,958</b> | <b>2,766</b> | <b>3,651</b> | <b>3,750</b> | <b>3,992</b> | <b>4,508</b> | <b>4,705</b>  |
| Inventory                     | 620          | 784          | 909          | 1,206        | 1,442        | 1,500        | 1,731        | 1,940         |
| Debtors                       | 373          | 527          | 568          | 714          | 1,081        | 1,248        | 1,523        | 1,708         |
| Cash & Bank                   | 206          | 791          | 127          | 167          | 167          | 249          | 1,057        | 1,332         |
| Other Current Assets          | 412          | 236          | 1,165        | 829          | 1,226        | 1,207        | 855          | 935           |
| <b>Current Assets</b>         | <b>1,612</b> | <b>2,338</b> | <b>2,769</b> | <b>2,915</b> | <b>3,915</b> | <b>4,205</b> | <b>5,166</b> | <b>5,915</b>  |
| Creditors                     | 306          | 466          | 580          | 741          | 961          | 962          | 1,015        | 1,138         |
| Provisions                    | 25           | 84           | 105          | 124          | 124          | 127          | 146          | 162           |
| Other Current Liabilities     | 188          | 327          | 388          | 352          | 537          | 430          | 492          | 552           |
| <b>Curr Liabilities</b>       | <b>519</b>   | <b>877</b>   | <b>1,073</b> | <b>1,217</b> | <b>1,622</b> | <b>1,519</b> | <b>1,653</b> | <b>1,852</b>  |
| <b>Net Current Assets</b>     | <b>1,094</b> | <b>1,461</b> | <b>1,695</b> | <b>1,698</b> | <b>2,293</b> | <b>2,685</b> | <b>3,512</b> | <b>4,063</b>  |
| <b>Total Assets</b>           | <b>4,348</b> | <b>5,296</b> | <b>5,535</b> | <b>6,568</b> | <b>7,666</b> | <b>8,208</b> | <b>9,674</b> | <b>10,620</b> |

### Income Statement

Fig in Rs Cr

| Y/E March                        | FY14         | FY15         | FY16         | FY17         | FY18         | FY19         | FY20E        | FY21E        |
|----------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| <b>Revenue from Operation</b>    | <b>3,131</b> | <b>3,743</b> | <b>5,048</b> | <b>5,853</b> | <b>6,431</b> | <b>7,357</b> | <b>8,422</b> | <b>9,443</b> |
| Change (%)                       |              | 20%          | 35%          | 16%          | 10%          | 14%          | 14%          | 12%          |
| <b>EBITDA</b>                    | <b>424</b>   | <b>422</b>   | <b>853</b>   | <b>999</b>   | <b>1028</b>  | <b>1115</b>  | <b>1540</b>  | <b>1604</b>  |
| Change (%)                       |              | -1%          | 102%         | 17%          | 3%           | 8%           | 38%          | 4%           |
| Margin (%)                       | 0            | 11.3%        | 16.9%        | 17.1%        | 16.0%        | 15.2%        | 18.3%        | 17.0%        |
| Depr & Amor.                     | 52           | 71           | 93           | 101          | 143          | 193          | 231          | 243          |
| <b>EBIT</b>                      | <b>373</b>   | <b>351</b>   | <b>760</b>   | <b>898</b>   | <b>885</b>   | <b>922</b>   | <b>1309</b>  | <b>1360</b>  |
| Int. & other fin. Cost           | 93           | 81           | 71           | 45           | 55           | 55           | 68           | 69           |
| Other Income                     | 169          | 181          | 240          | 112          | 96           | 88           | 113          | 145          |
| <b>EBT</b>                       | <b>449</b>   | <b>451</b>   | <b>928</b>   | <b>965</b>   | <b>926</b>   | <b>955</b>   | <b>1354</b>  | <b>1436</b>  |
| Exp Item                         | 0            | 0            | 0            | 0            | 0            | 0            | 0            | 0            |
| Tax                              | 10           | 59           | 176          | 60           | 288          | 181          | 103          | 172          |
| Minority Int & P/L share of Ass. | -            | -            | (11)         | (13)         | (7)          | -            | -            | -            |
| <b>Reported PAT</b>              | <b>439</b>   | <b>392</b>   | <b>742</b>   | <b>892</b>   | <b>631</b>   | <b>774</b>   | <b>1,251</b> | <b>1,264</b> |
| Change (%)                       |              | -11%         | 89%          | 20%          | -29%         | 23%          | 62%          | 1%           |
| Margin(%)                        | 14.0%        | 10.5%        | 14.7%        | 15.2%        | 9.8%         | 10.5%        | 14.9%        | 13.4%        |

## Financial Details

### Key Ratios

| Y/E March          | FY14  | FY15  | FY16  | FY17  | FY18  | FY19  | FY20E | FY21E |
|--------------------|-------|-------|-------|-------|-------|-------|-------|-------|
| ROE                | 16.5% | 13.1% | 20.1% | 20.0% | 13.0% | 14.2% | 19.2% | 16.7% |
| ROCE               | 12.9% | 11.6% | 19.9% | 19.3% | 17.7% | 16.3% | 19.2% | 17.5% |
| Asset Turnover     | 0.7   | 0.7   | 0.9   | 0.9   | 0.8   | 0.9   | 0.9   | 0.9   |
| Debtor Days        | 44    | 51    | 41    | 45    | 61    | 62    | 66    | 66    |
| Inv Days           | 72    | 76    | 66    | 75    | 82    | 74    | 75    | 75    |
| Payable Days       | 36    | 45    | 42    | 46    | 55    | 48    | 44    | 44    |
| Int Coverage       | 4     | 4     | 11    | 20    | 16    | 17    | 19    | 20    |
| P/E                | -     | -     | 22.0  | 29.6  | 37.5  | 27.1  | 23.9  | 23.7  |
| Price / Book Value | -     | -     | 4.4   | 5.9   | 4.9   | 3.9   | 4.6   | 4.0   |
| EV/EBITDA          | -     | (2)   | 19    | 26    | 23    | 19    | 19    | 18    |
| FCF per Share      | 156   | 16    | 39    | (15)  | (34)  | 21    | 39    | 74    |
| Div Yield          | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.8%  | 0.9%  | 0.6%  | 0.6%  |

### Cash Flow Statement

Fig in Rs Cr

| Y/E March                      | FY14         | FY15         | FY16         | FY17         | FY18         | FY19         | FY20E        | FY21E        |
|--------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| PBT                            | 449          | 451          | 928          | 965          | 926          | 955          | 1,354        | 1,436        |
| (inc)/Dec in Working Capital   | (65)         | (12)         | 10           | (263)        | (563)        | (143)        | (547)        | (265)        |
| Non Cash Op Exp                | 52           | 71           | 93           | 101          | 143          | 193          | 231          | 243          |
| Int Paid (+)                   | 14           | 77           | 67           | 61           | 55           | 55           | 68           | 69           |
| Tax Paid                       | (111)        | (106)        | (198)        | (264)        | (203)        | (251)        | (103)        | (172)        |
| others                         | (49)         | (156)        | (175)        | (129)        | (82)         | (31)         | 38           | -            |
| <b>CF from Op. Activities</b>  | <b>290</b>   | <b>325</b>   | <b>726</b>   | <b>471</b>   | <b>276</b>   | <b>777</b>   | <b>1,041</b> | <b>1,311</b> |
| (inc)/Dec in FA & CWIP         | (100)        | (135)        | (253)        | (634)        | (677)        | (527)        | (575)        | (424)        |
| Free Cashflow                  | 186          | 187          | 469          | (174)        | (408)        | 248          | 467          | 888          |
| (Pur)/Sale of Inv              | 2            | 103          | 32           | (42)         | 87           | 123          | (26)         | -            |
| others                         | 448          | (204)        | 423          | 390          | 223          | 89           | -            | -            |
| <b>CF from Inv. Activities</b> | <b>350</b>   | <b>(237)</b> | <b>202</b>   | <b>(286)</b> | <b>(367)</b> | <b>(314)</b> | <b>(601)</b> | <b>(424)</b> |
| inc/(dec) in NW                | -            | -            | -            | -            | 0            | -            | -            | -            |
| inc/(dec) in Debt              | (473)        | 87           | (671)        | 12           | 357          | (106)        | 239          | (328)        |
| Int. Paid                      | (91)         | (79)         | (71)         | (64)         | (55)         | (55)         | (68)         | (69)         |
| Div Paid (inc tax)             | (32)         | (57)         | (185)        | (86)         | (218)        | (219)        | (216)        | (216)        |
| others                         | (4)          | (3)          | -            | -            | -            | -            | -            | -            |
| <b>CF from Fin. Activities</b> | <b>(600)</b> | <b>(52)</b>  | <b>(927)</b> | <b>(138)</b> | <b>85</b>    | <b>(379)</b> | <b>(45)</b>  | <b>(613)</b> |
| Inc(Dec) in Cash               | 40           | 37           | 1            | 47           | (7)          | 84           | 395          | 274          |
| <b>Add: Opening Balance</b>    | <b>60</b>    | <b>103</b>   | <b>126</b>   | <b>119</b>   | <b>173</b>   | <b>165</b>   | <b>662</b>   | <b>1,057</b> |
| Closing Balance                | 101          | 140          | 127          | 167          | 167          | 249          | 1,057        | 1,332        |

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Correspondence Office Address: Arch Waterfront, 5th Floor, Block GP, Saltlake, Sector 5, Kolkata 700 091; Tel No.: 033-40541700; [www.narnolia.com](http://www.narnolia.com).

Registered Office Address: Marble Arch, Office 201, 2nd Floor, 236B, AJC Bose Road, Kolkata 700 020; Tel No.: 033-4050 1500; [www.narnolia.com](http://www.narnolia.com)

Compliance Officer: Manish Kr Agarwal, Email Id: [mkagarwal@narnolia.com](mailto:mkagarwal@narnolia.com), Contact No.:033-40541700.

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