



DEALMONEY SECTOR REPORT

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SECTOR OF THE MONTH PHARMA



PICKS OF
THE MONTH

#DR REDDY LABS LTD
#ALEMBIC PHARMA LTD

Sector of the Month: Pharma

India is leading pharma producer

India is a prominent and rapidly growing presence in global pharmaceuticals. It is the largest provider of generic medicines globally, occupying a 20% share in global supply by volume, and also supplies 50% of global demand for vaccines. India ranks 3rd worldwide for production by volume and 13th by value, thereby accounting for around 10% of world's production by volume and 1.5% by value. It supplies over 40 per cent of generic demand in the US and 25 per cent of all medicine in UK. India's pharmaceutical exports stood at US\$ 13.69 billion in FY20 (up to January 2020). The exports are expected to reach US\$ 22 billion by 2020. Indian pharmaceutical sector is expected to grow at a CAGR of 22.4 per cent in the near future and medical device market expected to grow US\$ 25 billion by 2025. India is the second largest contributor of global biotech and pharmaceutical workforce.

India is the source of 60,000 generic brands across 60 therapeutic categories and manufactures more than 500 different Active Pharmaceutical Ingredients (APIs). The Department of Pharmaceuticals aims to make the country a hub for end-to-end drug discovery under its 'Pharma Vision 2020'.

Advantage India

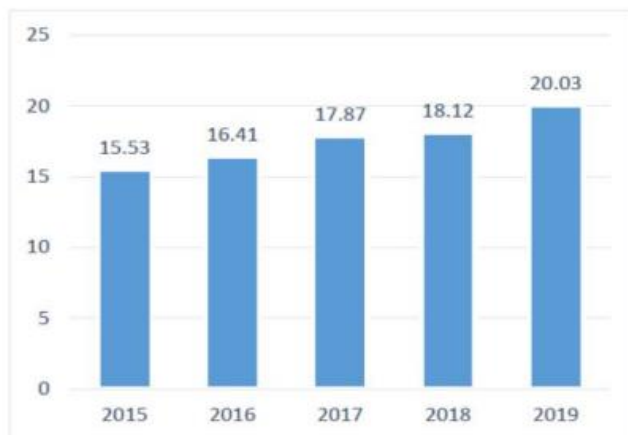
- From 2018-19, India's pharmaceuticals exports were worth US\$ 19.13 billion with a growth of 10.72 cent over \$17.28 billion in pharma exports last year
- Third largest Pharmaceuticals market by 2020 in terms of incremental growth
- The cost of manufacturing in India is approximately 33% lower than that of the US

Important Segments in Indian Pharmaceutical Sector



Source: Ace Equity, Dealmoney Research

Annual Turnover of Indian Pharmaceutical Market (US\$ billion)



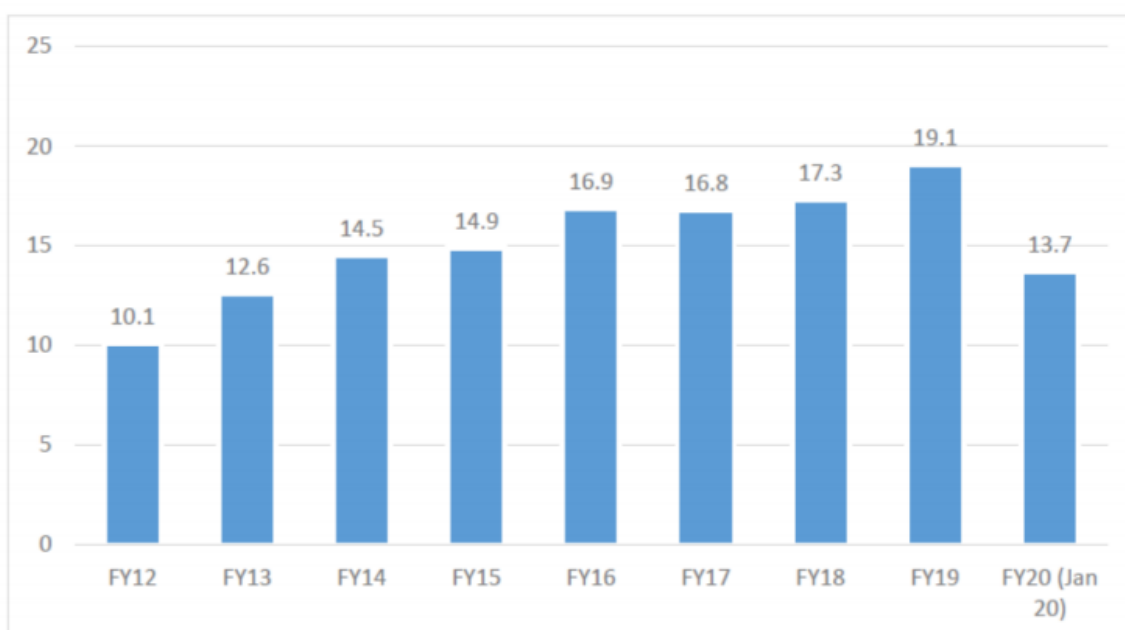
Quarterly Growth in Indian Pharma Market (%)



- India's domestic pharmaceutical market turnover reached Rs 1.4 lakh crore (US\$ 20.03 billion) in 2019, growing 9.8 per cent year-on-year (in Rs) from Rs 129,015 crore (US\$ 18.12 billion) in 2018.
- Medicine spending in India is projected to grow 9-12 per cent over the next five years, leading India to become one of the top 10 countries in terms of medicine spending.
- India's cost of production is significantly lower than that of the US and almost half of that of Europe. It gives a competitive edge to India over others

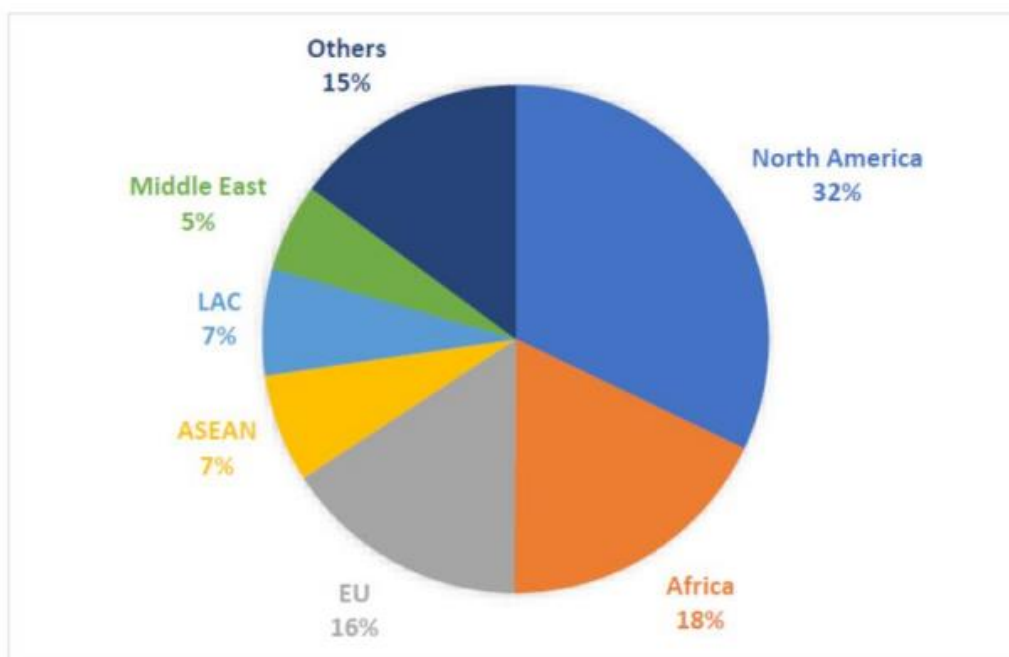
Pharma export to continue to grow

Pharmaceutical Exports from India (US\$ billion)



Source: Ace Equity, Dealmoney Research

Major Export Destinations in India's Pharma Export in FY19 (%)



India is the world's largest provider of generic medicines; the country's generic drugs account for 20 per cent of global generic drug exports (in terms of volumes). Indian drugs are exported to more than 200 countries in the world, with the US as the key market. Indian pharma companies are capitalising on export opportunities in regulated and semi-regulated markets. Pharmaceutical exports from India, which include bulk drugs, intermediates, drug formulations, biologicals, Ayush & herbal products and surgicals reached US\$ 19.14 billion in FY19 and US\$ 13.7 billion in FY20 (up to Jan 2020). The pharma export is estimated to touch US\$ 22 billion in FY20.

Has a potential to be a USD 55 Billion market by 2030

From a market size of USD 12.6 billion in 2009, the Indian pharmaceutical market will grow to USD 55 billion by 2020, with the potential to reach USD 70 billion in an aggressive growth scenario. In a pessimistic scenario characterised by regulatory controls and economic slowdown, the market will be depressed and is expected to reach USD 35 billion. With market diversity on the rise, the drivers of growth have proliferated and become more nuanced. We identified 11 drivers of growth grouped under four dimensions: epidemiological factors, increasing affordability, enhanced accessibility, and rising acceptability. Firstly, population growth at around 1.3 per cent every year and a steady rise in disease prevalence will increase the patient pool by nearly 20 per cent by 2020. Second, the affordability of drugs will rise due to sustained growth in incomes and increases in insurance coverage.

Source: Ace Equity, Dealmoney Research

Limited Impact of Covid-19 on Indian Pharma Sector

Indian pharmaceuticals market is likely to grow 3%-5% in size during FY20-21, despite the COVID-19 related lock-down and there would be monthly revenue improvements from June 2020, says India Ratings and Research (Ind-Ra).

The seasonality in the Indian domestic business will support the recovery. Together with continuous rise in the number of COVID-19 cases in India will result in further volume growth in related therapies. Furthermore, pharma companies' large cash balances and sufficient headroom under debt covenants along with diversified funding sources will mitigate any impact of the ongoing lock-down.

The COVID-19 impact on the pharma sector has been less pronounced than observed in the other sectors, as pharmaceuticals fall under the essential service category and sector companies are exempt from the restrictions under the nationwide lock-down.

Additionally, to avoid drug shortages, the government of India has removed the roadblocks in the movement of pharma products and ancillary supplies as well as employees engaged, thus aiding overall supplies. "Pharma companies with exposure to chronic therapies will witness a lower impact than the companies with exposure acute therapies as patients are curtailing their visits to doctors," Ind-Ra says.

Manufacturing volumes after declining to 50%-60% in April 2020, given the strict lock-down, has improved significantly to 60%-80% of the original capacities during May-June 2020, as per industry interactions of IndRa. The overall manufacturing activities had reduced, given the lack of manpower availability and lower availability of transportation for the staff in the initial days, it added. However, according to Ind-Ra, logistics remains a big challenge for pharma companies during the COVID-19 pandemic.

Ind-Ra also expect price hike by most pharma players in coming days. It says, "Companies may take price hikes on non-DPCO (drug price control order) products up to 8%, unlike the earlier average price hike of 5% (max limit 10%) due to an increase in raw material cost and the additional cost incurred towards raw materials, logistics and manpower. The annual price hikes by companies are generally taken during 1Q. The same is likely to result in improved profitability and cash flows.

Source: Ace Equity, Dealmoney Research

Pick of the Month (Dr Reddy Labs Ltd.):

CMP: 4858

Target: 5356

Dr. Reddy's Laboratories Limited provides a complete range of pharmaceutical services. The Company manufactures bulk drugs and formulations including verapamil and cephalexin. The Company also manufactures and exports molecules such as norfloxacin, ciprofloxacin, and varieties of semi-synthetic penicillin. The Company markets its products in India and around the world.

Strong Q2FY21 numbers: The revenues for DRREDDY grew by 2% YoY to Rs.4897 crs on account of new launches across market, volume traction in base business and integra on of business acquired at Wockhardt. Gross margin contracted 210bps to ~54% QoQ primarily on account of lower export incentives, adverse forex and generics price erosion, partially offset by new product launches. The decline in gross margin was offset by productivity gains across SG&A and R&D expenses.

Overall growth in its market: The overall Domestic business increased by 21% YoY to Rs.912 crs in 2QFY21 on account of increase market demand post COVID lockdowns, wockhardt acquisition and new product launches. The US business grew by 28% YoY to Rs.1833 crs in 2QFY21. The increase is because of new products, forex, volume uptake of selected molecule segment and to some extent offset of price erosion. The Europe business grew by 35% YoY to Rs 375 crs on account of improvement in base business and new product launches. The Emerging market business grew by 4% YoY to Rs.864 crs because of the 28 launches. Within EM segment the Russia business showed growth of 4% in constant currency. Pharmaceuticals Services and Active Ingredients (PSAI) business (+20% YoY) continued to benefit from stocking and broader sectoral tailwinds in the API segment

Valuations: With new sales momentum with growth in overall markets of US, Europe and EM along with strong growth in domestic market with expected launches of 17 new products. Increased productivity and plans to launch limited competition product could drive the growth in FY21 and 94 pending ANDAs approval by USFDA. We recommend buy on Dr Reddy Labs with a price target of Rs. 5356.

NSE/BSE Code	DRREDDY / 500124
Sector	Healthcare
Industry	Pharmaceuticals & Drugs
Face value/Book Value (Rs.per share)	2 / 979.5
Dividend yield(%)	0.5
52H/L(Rs.)	5515 / 2498
Market Cap.(Rs.mn)	8,12,136
Shares Outstanding (mn)	166.30

(In Rs. mn)	FY17	FY18	FY19	FY20
Net Sales	1,41,961	1,42,810	1,54,482	1,75,170
Sales Growth	-8.80%	0.60%	8.20%	13.40%
EBITDA	24,722	23,512	31,782	24,704
EBITDA Margin	17.40%	16.50%	20.60%	14.10%
PAT	12,572	9,124	19,062	19,699
PAT Margin	8.90%	6.40%	12.30%	11.20%
EPS (Rs)	77.9	57	117.5	121.9

	FY17	FY18	FY19	FY20
P/E (x)	64.6	89	42.6	41.2
P/B (x)	6.6	6.5	5.8	5.2
EV/Sales	5.7	5.6	5.2	4.6
EV/EBITDA	32.5	34.1	25.2	32.5
ROE	9.80%	8.20%	13.40%	10.80%
ROCE	10.20%	7.40%	14.40%	13.40%

Qtr Earnings (in Rs. cr)	Q2FY21	Q1FY21	Q-o-Q %	Q2FY20
Net Sales	4,776.60	4,417.50	8.1	3,998.20
Total Expenditure	3,754.80	3,305.20	13.6	3,749.00
PBIDT (Excl OI)	1,156.10	1,121.30	3.1	1,063.80
PAT	764.5	586.9	30.26	1095.1
PBIDTM% (Excl OI)	23.54	25.33	-7.07	22.1
PBIDTM%	24.58	27.3	-9.96	23.23
PATM%	15.57	13.26	17.42	22.75
Adj. EPS(Rs)	46.44	35.78	29.79	66.59

Source: Ace equity, IBEF, Dealmoney research

Pick of the Month (Alembic Pharma Ltd.):

Alembic Pharmaceuticals Limited is a pharmaceutical company. The Company is engaged developing formulations and active pharmaceutical ingredients (API). The Company focuses on anti-infective, analgesic and, cough and cold therapies. It also focuses on therapies, such as cardiology, diabetes, gynecology, gastrointestinal, orthopedic, dermatology and ophthalmology. Its APIs include independent manufacturing blocks for Macrolides, non-steroidal anti-inflammatory drugs (NSAIDs) and other drugs. The Company offers international and domestic formulations.

Upbeat quarterly growth: Alembic Pharmaceuticals Limited has registered a 35% growth in its PAT. Its revenue grew by 17.65% YoY to Rs 1457 crore led by strong growth in RoW and API segments, which grew 84.1% and 28.9% to Rs 197 crore and Rs 263 crore, respectively. Additionally, US formulations grew 8% to Rs 582 crore whereas domestic formulations grew 6.1% to Rs 415 crore.

US sales shows a bright spot for growth: Its US sales in Q2 FY21 grew 8% to Rs5.8bn due to strong performances in base products (including sartans) and launches. Six products were launched in H1 and 8-9 are planned to be launched in H2. Alembic is set to expand its product range as it reveals oncology (oral solids + injectables) and other complex generic pipelines currently being developed. We expect its US business to grow 15-18% over FY21-22.

Strong Traction in domestic business: Its domestic sales comprise 31% of the overall sales with higher contribution from specialty (54% of domestic sales). Its Q2 FY21 domestic formulations grew 6% y/y to Rs4.2bn due to the strong performances of key brands like Azithral. Management expects its Azithromycin market share to expand. We expect domestic formulations to clock an 6-8% revenue CAGR over FY21-23.

Valuations: With increased focus on niche filings in derma and oncology and Alembic has invested nearly Rs20bn in new capacities (Aleur, oncology, OSDs) to diversify its product range for the US. Currently, the stock is trading at 17.9x TTM PE. We recommend a buy at Rs.959 with the target of Rs. 1115.

CMP:967

Target: 1115

NSE / BSE Code	APLLTD / 533573
Sector	Healthcare
Industry	Pharmaceuticals & Drugs
Face value / Book Value (Rs per share)	2 / 241.2
Dividend yield (%)	1
52 H/L (Rs.)	1128 / 436
Market Cap. (Rs. mn)	1,88,504
Shares Outstanding (Cr)	196.60

(In Rs. mn)	FY17	FY18	FY19	FY20
Net Sales	31,346	31,302	39,347	46,058
Sales Growth	-1.00%	-0.10%	25.70%	17.10%
EBITDA	6,147	6,153	8,558	12,141
EBITDA Margin	19.60%	19.70%	21.80%	26.40%
PAT	4,069	4,209	5,926	8,006
PAT Margin	13.00%	13.40%	15.10%	17.40%
EPS (₹)	21.4	21.9	31	44

	FY17	FY18	FY19	FY20
P/E (x)	46.3	44.8	31.8	23.5
P/B (x)	9.9	8.5	6.9	5.9
EV/Sales	5.9	5.9	4.7	4
EV/EBITDA	30	30	21.6	15.2
ROE	28.90%	22.20%	22.70%	23.30%
ROCE	23.30%	20.40%	24.00%	27.00%

Qtr Earnings (in Rs. cr)	Q2FY21	Q1FY21	Q-o-Q %	Q2FY20
Net Sales	1,457.10	1,341.30	8.6	1,240.90
Total Expenditure	1,013.70	934.00	8.5	895.40
PBIDT (Excl OI)	443.40	407.40	8.9	345.50
PAT	325.41	292.74	11.16	250.37
PBIDTM% (Excl OI)	30.43	30.37	0.2	27.84
PBIDTM%	30.65	30.39	0.86	27.87
PATM%	22.33	21.82	2.34	20.18
Adj. EPS(Rs)	16.96	15.55	9.07	13.06

Source: Ace equity, IBEF, Dealmoney research

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