

LAURUS LABS LIMITED

**IPO Note
(Neutral)**

Analyst:

Rohit Rai

Sumeetkumar Jain, CMT

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IPO details

Key Data	
Issue Opens	6-Dec-16
Issue Closes	8-Dec-16
Equity Shares Offered (in mn.)	31.10
QIB	Up to 50%
NIB	Min 15%
Retail	Min 35%
Face Value (₹)	10
Price Band (₹)	426-428
Max. Issue Size (₹ mn)	13,311
Lot Size (Eq. Shares)	35 and multiple thereof

Valuation	@ ₹426 per share	@ ₹428 per share
Market Cap (₹ mn)	45,052	45,264
Net Debt (₹ mn)	10,278	10,278
Enterprise Value (₹ mn)	55,330	55,542
EV/ Sales	3.1	3.1
EV/ EBIDTA	15.1	15.1
P/B	5.3	5.3
P/E	34.0	34.1

Source: Red Herring Prospectus, Destimoney Research

	Pre Issue		Post Issue [^]	
	# mn Shares	% Holding	# mn Shares	% Holding
Promoters	32.4	32.8%	32.4	30.6%
Public	66.3	67.2%	42.2	39.9%
Offer For Sale			24.1	22.8%
New Issue			7.0	6.6%
Total	98.7	100.00%	105.8	100.0%

Object of Offer for sale

- To enhance company's visibility and brand
- Pre-payment of term loans.
- General corporate purposes.

[^]NOTE: Valuation Parameters considered are fully subscribed issue for FY16 financials

- ❑ Laurus Labs Limited (Laurus Labs) is an leading research and development (“R&D”) driven pharmaceutical company in India, with a leadership position in generic active pharmaceutical ingredients (“APIs”) for select, high-growth therapeutic areas of anti-retrovirals (“ARVs”) and Hepatitis C.
- ❑ Laurus Labs operates in four business lines: Generics – APIs, Generics – FDFs, Synthesis and Ingredients. Generics – API business comprises the development, manufacture and sale of APIs and advanced intermediates; Generics – FDF business comprises the development and manufacture of oral solid formulations; Synthesis business includes contract development and manufacturing services for global pharmaceutical companies; and Ingredients business comprises the manufacture and sale of specialty ingredients for use in the nutraceutical and cosmeceutical sectors.
- ❑ Laurus Labs is focused on growing their presence in the key therapeutic areas, comprising ARV, Hepatitis C and Oncology. Laurus Labs has launched 59 products since their inception in 2005.
- ❑ Laurus Labs key customers include Aspen Pharmacare Limited, Aurobindo Pharma Limited, Cipla Limited, Mylan Laboratories Limited, NATCO Pharma Limited (“NATCO”) and Strides Shasun Limited. For the financial year 2016, nine out of the 10 largest generic pharmaceutical companies in the world, by revenue, were Laurus Labs customers.
- ❑ Laurus Labs has delivered consistent growth over the last five financial years both in terms of financial and operational metrics. Total revenues, on a standalone basis, have grown at a CAGR of 41.0% from ₹4,523.07 million for the financial year 2012 to ₹17,884.15 million for the financial year 2016 and restated profit for the year, on a standalone basis, it has grown at a CAGR of 60.6% from ₹215.77 million for the financial year 2012 to ₹1,435.68 million for the financial year 2016.
- ❑ The business offers an opportunity for the investors to participate in the growth of the company as rising demand for its products in the market of ‘API’ and growth of its different portfolio in the market. Though we feel the pricing is on an UPPER SIDE, considering company’s current financials and a declining ROE, high product risk 92% revenue from APIs and high client concentration (top 10 client contributes 78% of sales) does not give us valuation comfort. We also do not expect any immediate listing gains. Though higher P/E ratio than its peers i.e Divis Laboratories and Aurobindo Pharma which are in sub 30 levels, we are **NEUTRAL** to the IPO listing.

Source: Red Herring Prospectus, ACE Equity

Strengths of Laurus Labs

- ❑ **Leadership in APIs in Select, High Growth Therapeutic Areas** its key products for ARV therapy include EFV, TDF, 3TC and FTC. Its is well positioned to capitalize on the ARV API opportunity as a result of its portfolio and scale of operations.
- ❑ **Strong R&D Capabilities and Process Chemistry Skills** as of June 30, 2016, the Company owned 32 patents and had 150 pending patent applications, in several countries, and have commercialized 59 products. The Company's total expenditure for R&D activities, including for product development costs, was ₹906.52 million for the financial year 2016 compared to ₹586.49 million for the financial year 2015 and ₹424.40 million for the financial year 2014. As of June 30, 2016, it employed 599 scientists at its R&D centers, which constituted 25.0% of its total employee strength.
- ❑ **Industry Leading, Modern and Regulatory Compliant Manufacturing Capacities** it has three manufacturing facilities in Visakhapatnam and a kilo lab facility in Hyderabad, which have received one or more approvals from WHO, US FDA, PMDA, NIP Hungary, KFDA or BfArM. In order to meet the growing demand for products, It has increased the aggregate reactor volume of facilities to 1,833.6 KL, as of June 30, 2016. Post planned expansion, its aggregate reactor volume will increase to 2,095.6 KL during the financial year 2017.
- ❑ **Long-standing Relationships with Multi-National Pharmaceutical Companies** has maintained long-standing relationships with multi-national pharmaceutical companies. Laurus Labs top five customers have been with them for at least five years and these customers, in aggregate, contributed to approximately 67.8% of total revenue and its cumulative revenue from such customers has grown year over year for the last three financial years.
- ❑ **Experienced Promoters and Qualified Operational Personnel** its core managerial team has an average pharmaceutical industry experience of more than 20 years and almost all of them have been associated with the company since its formative years.

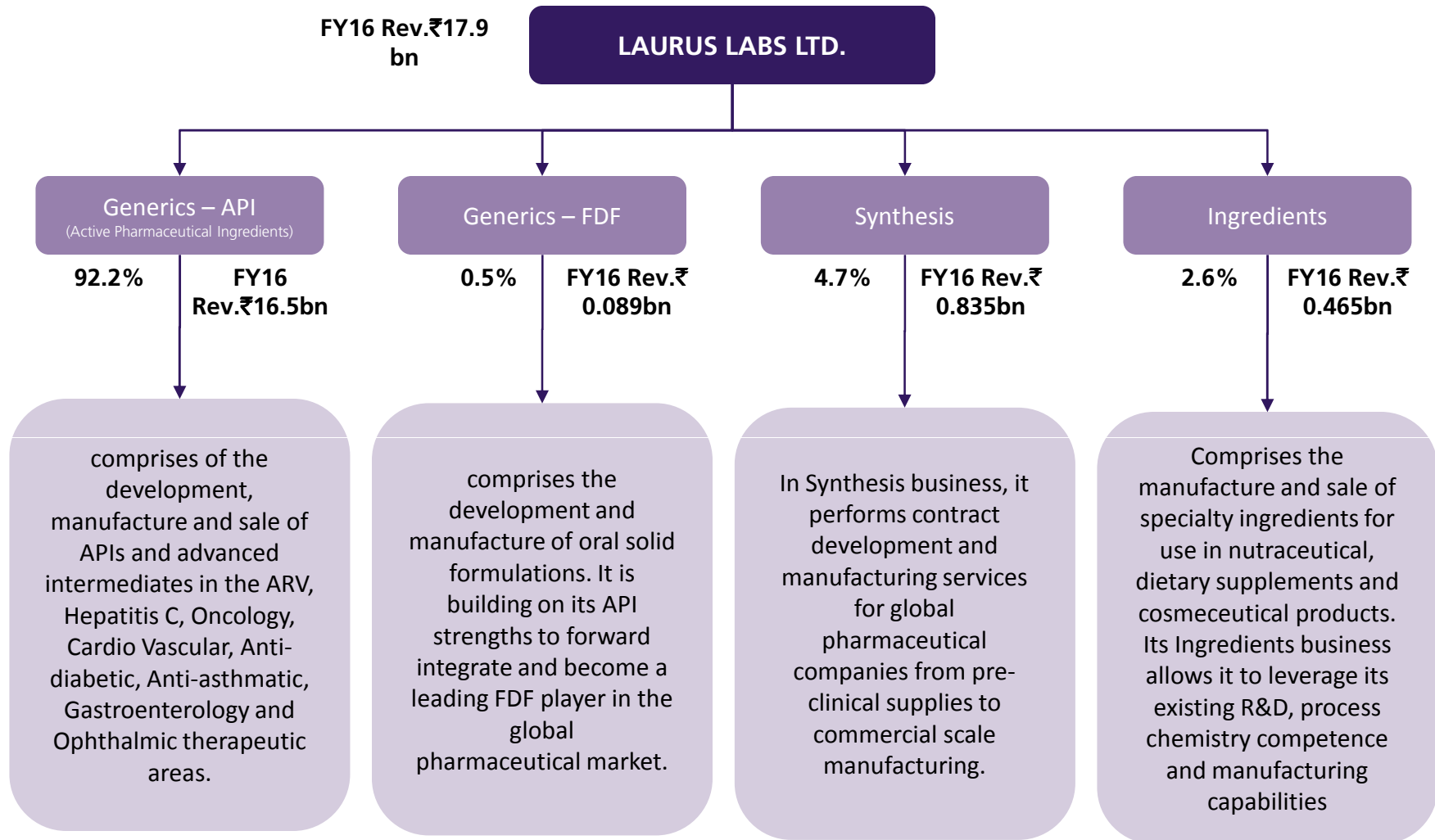
Source: Red Herring Prospectus, ACE Equity

Future road ahead

- ❑ **To capitalize on its Leadership Position in APIs in Select, High-Growth Therapeutic Areas** there are significant growth opportunities in this area as a result of expected increase in the HIV patient pool with the current WHO guidelines recommending initiating early treatment for infected HIV patients, regardless of age and viral load. At the end of 2015, approximately 17 million people were receiving antiretroviral therapy of the total 36.7 million people living with HIV globally, representing approximately 46% of the total HIV population.
- ❑ **Expanding its API Portfolio** as it has developed several products in the anti-diabetic, cardio vascular and gastroenterology therapeutic areas and are currently in the process of setting up dedicated capacities to manufacture products in these therapeutic areas at our Unit 3 manufacturing facility.
- ❑ **Leverage API Cost Advantage for Forward Integration into Generic Finished Dosage Formulation (FDF)** the Company had spent ₹906.52 million towards our R&D activities and ₹2,013.66 million to set up a FDF manufacturing facility and intend to further increase our R&D and manufacturing capacities and expertise in development, manufacture and sale of oral solid formulations, which we believe offers significant growth opportunities in ARVs, Anti-diabetic, Cardio Vascular and Hepatitis C therapeutic areas.
- ❑ **Develop its Synthesis Business** with a view to develop its pipeline for clinical phase manufacturing of new chemical entities and contribute to the supply chain of its customers, it has established a presence in Greater Boston, Massachusetts, in 2015 with 12 scientists and four sales personnel who are focused on strengthening its synthesis business. It intends to focus more on the supply of key starting materials and intermediates for new chemical entities as the molecules move to Phase III and to a commercial stage, which would result in significant revenue.
- ❑ **Strengthen its Ingredients Business** it currently develops and manufactures specialty ingredients for use in nutraceutical, dietary supplements and cosmeceutical products. The nutraceutical and cosmeceutical sectors are undergoing consolidation globally and implementing quality standards similar to that of the pharmaceutical industry. Because of the implementation of such quality standards, it intends to leverage its strong process chemistry skills to strengthen presence in the nutraceutical and cosmeceuticals sectors in the manufacture of nature identical substances.

Source: Red Herring Prospectus, ACE Equity

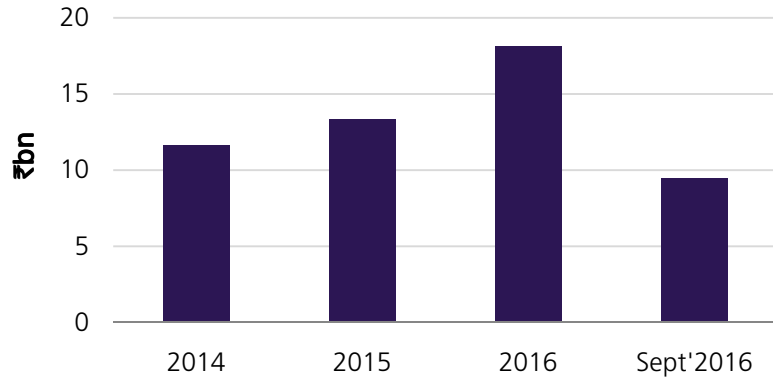
Generic – API forms major part of Laurus Labs revenue



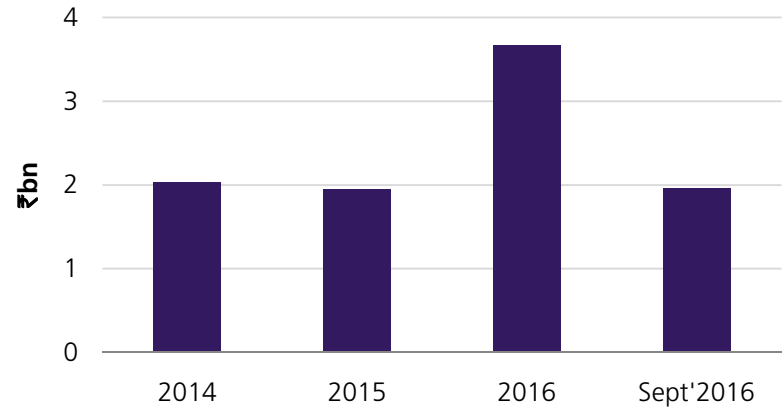
Source: Red Herring Prospectus

It has shown a growth in its revenue consistently

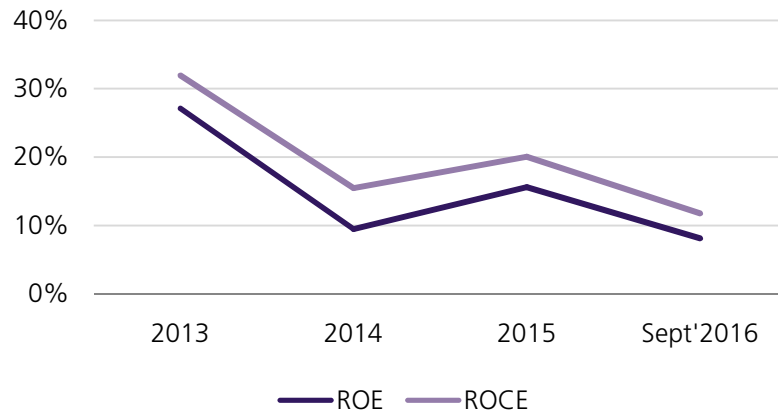
Revenue Trend



Operating Profit



Declining Return Ratio Profile



Source: Red Herring Prospectus, ACE Equity

Has a higher P/E than its listed peers

Name	Revenue ₹ mn	P/E	ROE %	ROCE %
Divis Laboratories	37,764	29.16	28.57	35.18
Aurobindo Pharma Limited	138,961	22.89	32.17	27.89
Laurus Labs Limited	17,838	34.1	15.6	20.1

Source: Red Herring Prospectus, ACE Equity

Consolidated Summary Financials

Income Statement

₹ mn	As at Sept FY16	FY16	FY15	FY14
Total Income	9,296	17,838	13,266	11,597
COGS	5,316	10,252	9,057	7,907
Operating Expense	2,014	3,915	2,257	1,654
EBIDTA	1,966	3,671	1,951	2,036
Interest & Fin. Charges	529	1,149	1,011	587
Depreciation	536	922	615	329
Other Income	122	76	341	88
Exceptional items	-	-	-	-
PBT	1,023	1,676	666	1,209
Tax	258	345	(16)	236
PAT	766	1,331	681	972
Share of Associate	(15)	(4)	2	-
Net Profit	751	1,327	684	972

₹ mn	As at Sept FY16	FY16	FY15	FY14
Gross Margin	42.8%	42.5%	31.7%	31.8%
EBIDTA Margin	21.2%	20.6%	14.7%	17.6%
Net Margin	8.1%	7.4%	5.2%	8.4%
ROE	8.1%	15.6%	9.5%	27.1%
ROCE	11.8%	20.1%	15.4%	31.9%

Balance Sheet

₹ mn	As at sept FY16	FY16	FY15	FY14
Liabilities				
Share capital	987	824	821	778
Share Warrants & Outstandings	-	27	29	34
Reserves and surplus	8,302	7,668	6,370	2,772
Minority Interest	-	-	-	-
Deferred tax liabilities	597	448	103	118
Other long term liabilities	385	442	447	-
Long term provisions	76	68	51	39
Long term borrowings	2,829	4,606	3,037	1,882
Trade payables	3,083	2,493	2,308	2,275
Other current liabilities	3,537	1,445	1,333	1,643
Short-term borrowings	5,758	4,814	4,316	3,122
Short-term provisions	251	196	67	70
Total Liabilities	25,805	23,030	18,883	12,732
Assets				
Net Block	10,592	10,856	8,010	4,993
CWIP	2,164	696	1,097	1,161
Intangible assets	-	-	-	-
Long term loans and advances	1,519	1,285	939	685
Non- Current Investment	56	70	74	-
Other non-current assets	137	83	123	128
Inventories	5,214	4,871	4,755	3,281
Trade receivables	5,333	4,449	2,851	1,949
Cash & bank balances	135	277	589	232
Short-term loans and advances	394	239	228	198
Other Current Assets	260	195	201	88
Misc Exp	-	9	16	17
Total Assets	25,805	23,030	18,883	12,732

Source: Red Herring Prospectus

Shareholding of Key management personnel

Name	No. of Equity Shares	Percentage of shareholding (%)
Dr. Satyanarayana Chava	16,781,704	16.99
Dr. Raju Srihari Kalidindi	5,200,000	5.27
Ravi Kumar V V	1,600,000	1.62
Dr. Lakshmana Rao C V	2,300,000	2.33
Dr. GSR Anjaneyulu	260,000	0.26
M Bhaskaraiah	120,000	0.12
Srinivasa Rao S	120,000	0.12
Martyn Oliver James Peck	80,000	0.08

Source: Red Herring Prospectus, ACE Equity

Key Risks

- ❑ Laurus Labs derive a significant portion of revenue from the sale of products in certain therapeutic areas and any reduction in demand for these products could have an adverse effect on its business, results of operations, financial condition and cash flows.
- ❑ Any manufacturing or quality control problems may subject it to regulatory action, damage its reputation and have an adverse effect on its business, results of operations, financial condition and cash flow.
- ❑ Laurus Labs products may become obsolete due to a breakthrough in the development of alternate drugs.
- ❑ Laurus Labs derives a significant portion of its revenue from a few customers, most of whom it does not have long term contractual arrangements with, and the loss of one or more such customers, the deterioration of their financial condition or prospects, or a reduction in their demand for its products can have an adverse effect.

Destimoney Securities Private Limited

6th Floor, " A " Wing , Tech-Web Centre, New Link Road, Oshiwara , Near Behram Baug, Jogeshwari (West), Mumbai - 400102

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