

**BSE Code: 539523**
**NSE Code: ALKEM**
**Reuters Code: ALKE:NS**
**Bloomberg Code: ALKEM:IN**

### Poised for robust growth

Alkem Labs is a leading Indian pharmaceutical company engaged in the manufacturing of branded generics, generic drugs, active pharmaceutical ingredients ("APIs") and Nutraceuticals. Indian business contributes 73% to overall sales while international business contributes for the rest.

### Investment Rationale

🌀 **Domestic business to outperform the IPM growth:** Alkem has a comprehensive portfolio of over 700 brands spanning across major therapeutic segments such as Anti-infectives (42% of sales), Gastro-intestinal (18% of sales), Pain / Analgesics (12% of sales) and Vitamins / Minerals (8% of sales). The company has been consistently outperforming the IPM over the past ten years with improving market share in Anti-infectives (12% market share), Gastro-intestinal (6% market share) and Pain / Analgesics (5% market share). Importantly during FY16, 5 of the company's leading brands were featured among the top 50 while 14 brands were among the top 300 in the Indian pharmaceutical industry.

### .....Robust strategy to help overcome regulatory hurdles

Given the company's strong presence in the domestic formulation space, the regulatory headwinds related to NLEM (National List of Essential Medicines) and ban on FDC (fixed-dose combination) products are bound to impact revenues in FY17. However, Alkem has a robust strategy in place to overcome these hurdles. The company on one hand is consolidating its position in the established acute therapies and other hand expanding presence through new launches in the fast-growing chronic therapies (53 new products launched during FY16) while also taking price hikes. We believe all these initiatives will enable Alkem to report strong growth in FY18/19E and hence, we expect domestic business to grow at a CAGR of 17% over FY16-19E.

### 🌀 US to drive the exports revenue

US is a major contributor to international formulations & thus is a key focus market for the company. The company is witnessing strong demand for its products and is well placed to capitalize on the market opportunities given its established front end. Further, it has a healthy product pipeline of 77 ANDAs (31 of these are Para IV filings) and will continue to file 12-15 ANDAs every year. With this, the advantages of GDUFA (Generic Drug User Fee Act) system in terms of reducing approval timelines will lead to more product launches going forward and revenue to grow at a CAGR of 22.3% over FY16-19E.

**Valuation:** We expect revenue and PAT to grow at a CAGR of 18.5 & 21.7% respectively over FY16-19E. Further, EBITDA margin is expected to improve by 280bps on account of increasing launches in chronic products coupled with consolidation in acute therapies. Hence, we initiate Alkem with a BUY rating with a TP of Rs.1926 based on 19x FY19E EPS.

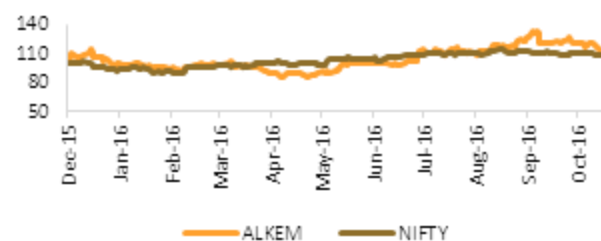
### Market Data

<b>Rating</b>	<b>BUY</b>
<b>CMP (Rs.)</b>	1,637
<b>Target (Rs.)</b>	1,926
<b>Potential Upside</b>	18%
<b>Duration</b>	Long Term
Face Value (Rs.)	2.0
52 week H/L (Rs.)	1,853/1,175
Adj. all time High (Rs.)	1,853
Decline from 52WH (%)	11.6
Rise from 52WL (%)	39.0
Beta	0.7
Mkt. Cap (Rs.Cr)	19,577

### Fiscal Year Ended

Y/E	FY16	FY17E	FY18E	FY19E
Net sales (Rs.Cr)	4,876.9	5,711.1	6,762.2	8,116.9
Adj. profit (Rs.Cr)	673	878	956	1,212
EPS (Rs.)	56.3	73.4	80.0	101.4
P/E (x)	29.1	22.3	20.5	16.2
P/BV (x)	5.6	4.7	3.9	3.3
ROE (%)	20.7	22.8	20.8	22.1

### One year Price Chart

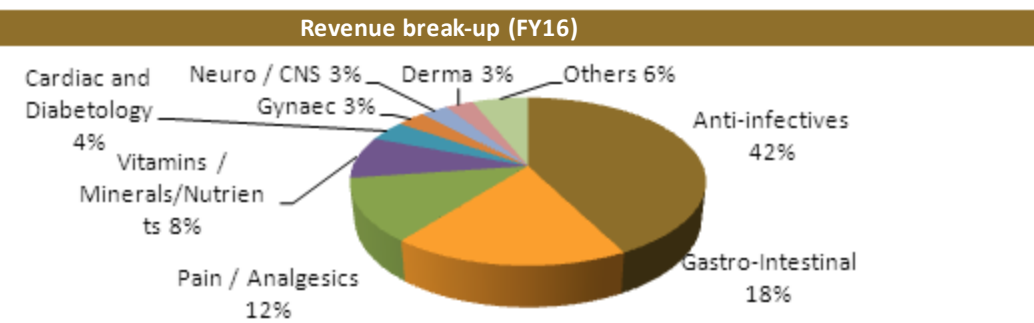


### Shareholding Pattern

Shareholding Pattern	Sept-16	Jun-16	Chg.
Promoters (%)	66.8	66.8	0
Public (%)	33.2	33.2	0

## Company Overview

Alkem Labs, a leading Indian pharmaceutical company is engaged in the manufacturing of branded generics, generic drugs, active pharmaceutical ingredients (“APIs”) and Nutraceuticals. Indian business contributes 73% to overall sales while international business contributes the rest. Alkem markets its products in India and 55 countries internationally. The company has 16 manufacturing facilities - 14 in India and 2 in the US (6 of its facilities are USFDA approved). Some of the company’s manufacturing plants enjoy fiscal benefits that are available for different periods.



Source: Company, In-house research

## Domestic business: On strong foothold despite regulatory headwinds

The company is the fifth largest pharmaceutical company and is also the third fastest growing company among the top ten pharmaceutical companies in the Indian domestic formulations market. The Indian formulations business contributed 72.5% to total revenues in FY16 and grew at a CAGR of 19.4% over FY11-16 led by mainly led by strong growth in acute products. In FY16, domestic business reported 30.3% growth vs. Indian pharmaceutical market (IPM) growth of 13.5%. Alkem’s domestic business comprises of established therapies and emerging therapies. The established therapies consist of anti-infectives; gastrointestinal; pain and analgesics; vitamins, minerals and nutrients, which together account for 80% of the total domestic sales. The company has been outperforming the market consistently in these therapies led by market share gains and new product introductions. The emerging therapies (comprise of Neuro/CNS, Derma, Cardiac and Anti-diabetes) contribute just 10% to the domestic sales however there is huge scope for growth on account of increasing chronic ailments.

Alkem has a comprehensive portfolio of over 700 brands spanning across major therapeutic segments such as Anti-infectives (42% of sales), Gastro-intestinal (18% of sales), Pain / Analgesics (12% of sales) and Vitamins / Minerals (8% of sales). The company has been consistently outperforming the IPM over the past ten years with improving market share in Anti-infectives (12% market share), Gastro-intestinal (6% market share) and Pain / Analgesics (5% market share). Importantly during FY16, 5 of the company’s leading brands were featured among the top 50 while 14 brands were among the top 300 in the Indian pharmaceutical industry.

### Alkem’s top therapies Market size in India (FY16)

	Rs. Cr
Anti-infectives	11,300
Gastro-intestinal	9,800
Pain/Analgesics	7,100
Vitamins/Minerals/Nutrients	7,000

Source: Company, In-house research

### Company's Therapeutic performance

Therapeutic area	Alkem rank	Alkem's sales in Rs. Cr	Mkt. share	Mkt. size in Rs. Cr	Company's CAGR	Market CAGR
	<b>FY15</b>				<b>FY11-15</b>	
Anti-infectives	1	1,191	11.2%	10,555	10.1%	6.8%
Gastro-intestinal	3	467	5.6%	8,409	17.5%	12.8%
Pain/Analgesics	3	312	5.0%	6,269	12.0%	10.9%
Vitamins/Minerals	6	225	3.7%	6,018	19.1%	12.1%
Gynaecology	9	100	2.4%	4,226	11.2%	10.4%
Respiratory	18	95	1.5%	6,463	8.3%	11.4%
Neuro/CNS	15	90	1.9%	4,662	33.7%	12.8%
Derma	15	76	1.5%	5,087	36.8%	17.5%
Cardiac	31	46	0.5%	9,022	40.1%	13.3%
Anti-diabetic	29	45	0.7%	6,232	69.7%	21.1%
Others	NA	72	0.8%	9,439	21.1%	12.3%

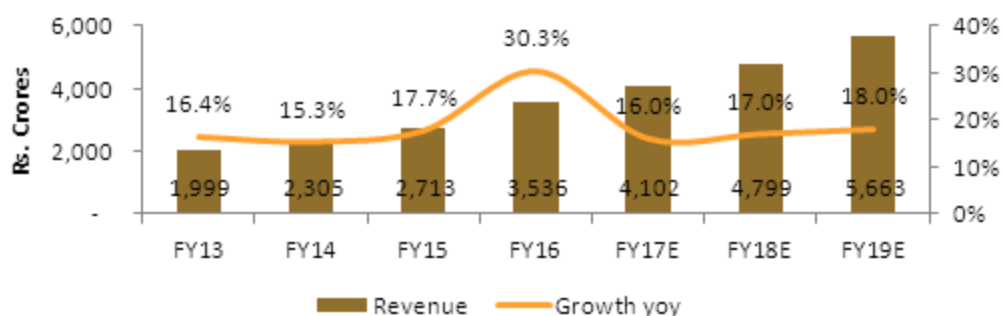
Source: Company, In-house research

Given the company's strong presence in the domestic formulation space, the regulatory headwinds related to NLEM (National List of Essential Medicines) and ban on FDC (fixed-dose combination) products are bound to impact revenues in FY17. However, Alkem has a robust strategy in place to overcome these hurdles. The company on one hand is consolidating its position in the established acute therapies and other hand expanding presence through new launches in the fast-growing chronic therapies (53 new products launched during FY16) while also taking price hikes. We believe all these initiatives will enable Alkem to report strong growth in FY18/19E and hence, we expect domestic business to grow at a CAGR of 17% over FY16-19E.

Therapeutic Areas	Rank FY16	Market Share (FY 2016)	Annual sales range (In Rs. Cr)
Anti-infectives	1	12%	>200
Gastro intestinal	3	6%	150-200
Pain/Analgesics	3	5%	50-150
Vitamins/Minerals/Nutrients	5	4%	25-50

Source: Company, In-house research

### Domestic business to grow at a CAGR of 17% during FY16-19E

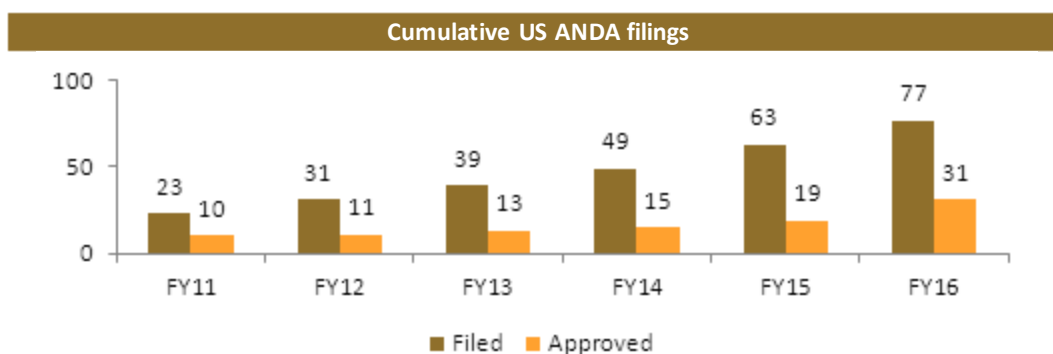


Source: Company, In-house research

### International business: Poised for strong growth

US is a major contributor to international formulations & thus is a key focus market for the company. The company is witnessing strong demand for its products and is well placed to capitalize on the market opportunities given its established front end. Further, it has a healthy product pipeline of 77 ANDAs (31 of these are Para IV filings) and will continue to file 12-15 ANDAs every year. With this, the advantages of GDUFA (Generic Drug User Fee Act) system in terms of reducing approval timelines will lead to more product launches going forward and revenue to grow at a CAGR of 22.3% over FY16-19E.

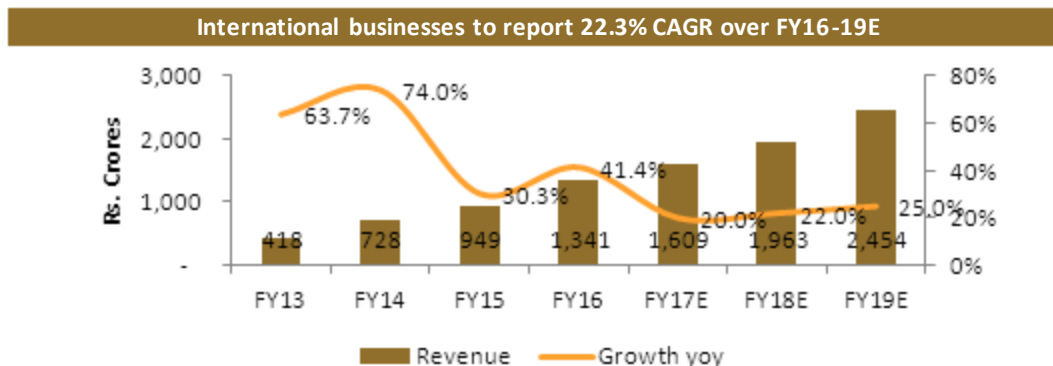
Apart from US, the company also has presence in other markets such as Australia, Europe, South East Asia, Latin America, Africa and CIS. Though US is the key market for Alkem, the company is focusing on select other international markets to create strong local presence with required infrastructure and is developing capabilities to exploit growth opportunities.



Source: Company, In-house research

### Acquisition of manufacturing facility to deepen its presence in US

In June 2015, the company acquired a formulation manufacturing facility along with its R&D capabilities from Long Pharmaceuticals LLC, in the US. This acquisition supports the company in diversifying its manufacturing footprint and also provides it with manufacturing capabilities in dosage forms like semi-solids, liquid and nasal formulations. The company is further scaling up the manufacturing capacity as it looks to file ANDAs in niche areas. Hence, we expect International revenue to grow at a CAGR of 22.3% over FY16-19E.



Source: Company, In-house research

### Key Risks:

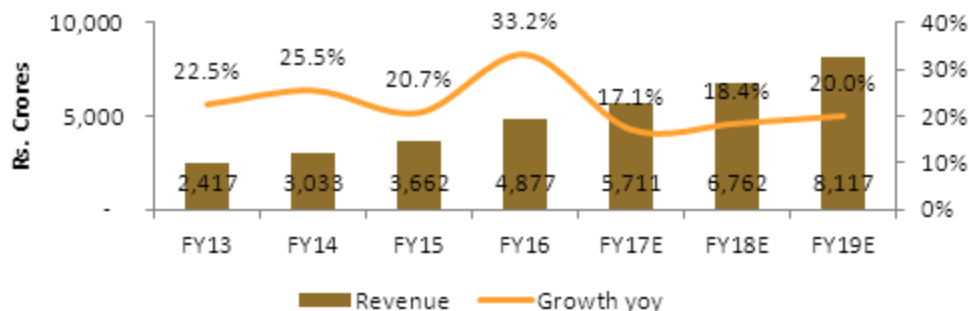
- New drugs inclusion in NLEM and FDC list.
- USFDA inspections and delay in key ANDA approvals.

## Financials

### Revenue to grow at CAGR of 18.5% with EBITDA margin expansion of 280 bps

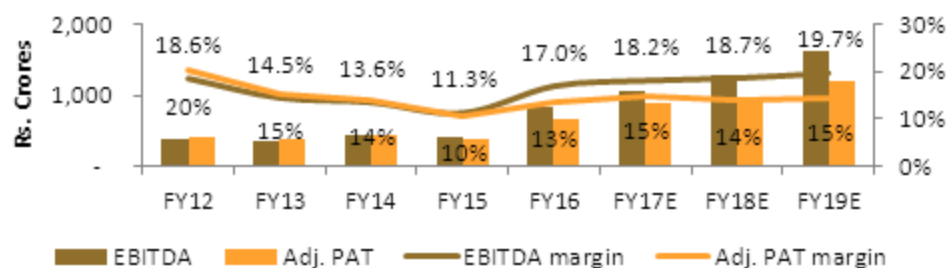
We expect revenue to grow at a CAGR of 18.5% over FY16-19E driven by: 1) consolidation of its leadership position in acute therapies 2) increasing presence in chronic therapies through new product launches 3) strong growth in US. Further, we expect EBITDA margin to expand by 280bps over FY16-19E led by improving profitability in chronic therapies & shift to non-FDC products. Hence, we expect PAT to grow at a CAGR of 21.7% over FY16-19E.

#### Revenue to grow at a CAGR of 17% over FY16-19E



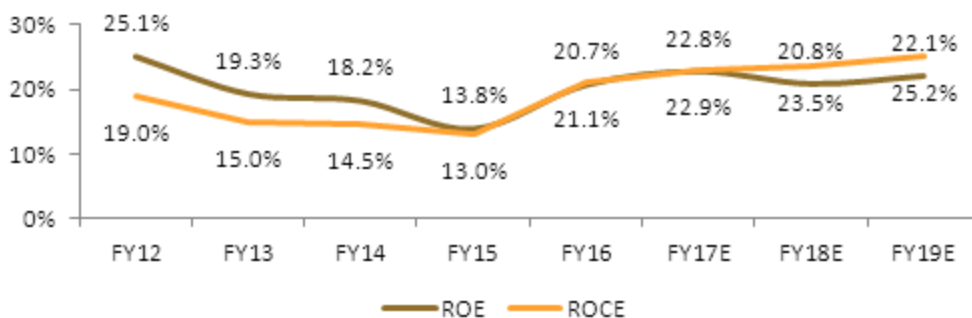
Source: Company, In-house research

#### EBITDA & PAT margin to improve by 280 bps, 110 bps respectively



Source: Company, In-house research

#### Return ratios trend



Source: Company, In-house research

**Profit & Loss Account (Consolidated)**

Y/E (Rs. Cr)	FY16	FY17E	FY18E	FY19E
<b>Total operating Income</b>	<b>4,992</b>	<b>5,845</b>	<b>6,921</b>	<b>8,308</b>
Raw Material cost	1,961	2,264	2,647	3,096
Employee cost	917	1,028	1,217	1,461
Other operating expenses	1,265	1,492	1,765	2,110
<b>EBITDA</b>	<b>848</b>	<b>1,061</b>	<b>1,292</b>	<b>1,640</b>
Depreciation	101	148	178	202
<b>EBIT</b>	<b>748</b>	<b>914</b>	<b>1,114</b>	<b>1,438</b>
Interest cost	67	45	45	45
Other Income	165	142	142	142
<b>Profit before tax</b>	<b>845</b>	<b>1,011</b>	<b>1,212</b>	<b>1,535</b>
Tax	161	121	242	307
<b>Profit after tax</b>	<b>685</b>	<b>890</b>	<b>969</b>	<b>1,228</b>
Minority Interests	11	12	13	16
P/L from Associates	-	-	-	-
<b>Adjusted PAT</b>	<b>673</b>	<b>878</b>	<b>956</b>	<b>1,212</b>
E/o income / (Expense)	-	-	-	-
<b>Reported PAT</b>	<b>673</b>	<b>878</b>	<b>956</b>	<b>1,212</b>

**Balance Sheet (Consolidated)**

Y/E (Rs. Cr)	FY16	FY17E	FY18E	FY19E
Paid up capital	24	24	24	24
Reserves and Surplus	3,482	4,176	4,950	5,979
<b>Net worth</b>	<b>3,506</b>	<b>4,200</b>	<b>4,974</b>	<b>6,003</b>
Minority interest	97	108	121	138
Total Debt	655	655	655	655
Other non-current liabilities	175	183	183	183
<b>Total Liabilities</b>	<b>4,432</b>	<b>5,147</b>	<b>5,934</b>	<b>6,979</b>
Total fixed assets	1,089	1,513	1,766	1,914
Capital WIP	172	180	100	100
Goodwill	353	353	353	353
Investments	422	422	422	422
Net Current assets	1,512	1,786	2,401	3,298
Deferred tax assets (net)	-	8	8	8
Other non-current assets	884	884	884	884
<b>Total Assets</b>	<b>4,432</b>	<b>5,147</b>	<b>5,934</b>	<b>6,979</b>

**Cash Flow Statement (Consolidated)**

Y/E (Rs. Cr)	FY16	FY17E	FY18E	FY19E
<b>Pretax profit</b>	<b>845</b>	<b>1,011</b>	<b>1,212</b>	<b>1,535</b>
Depreciation	101	148	178	202
Chg. in Working Capital	(30)	(142)	(194)	(218)
Others	8	(97)	(97)	(97)
Tax paid	(198)	(121)	(242)	(307)
<b>Cash flow from operating activities</b>	<b>726</b>	<b>797</b>	<b>856</b>	<b>1,115</b>
Capital expenditure	(257)	(580)	(350)	(350)
Chg. in investments	32	-	-	-
Other investing cashflow	411	142	142	142
<b>Cash flow from investing activities</b>	<b>186</b>	<b>(438)</b>	<b>(208)</b>	<b>(208)</b>
Equity raised/(repaid)	-	-	-	-
Debt raised/(repaid)	(671)	-	-	-
Dividend paid	(185)	(183)	(183)	(183)
Other financing activities	(71)	(45)	(45)	(45)
<b>Cash flow from financing activities</b>	<b>(927)</b>	<b>(228)</b>	<b>(228)</b>	<b>(228)</b>
Net chg in cash	(15)	132	420	679

**Key Ratios (Consolidated)**

Y/E	FY16	FY17E	FY18E	FY19E
<b>Valuation(x)</b>				
P/E	29.1	22.3	20.5	16.2
EV/EBITDA	23.0	18.3	14.7	11.2
EV/Net Sales	4.0	3.4	2.8	2.3
P/B	5.6	4.7	3.9	3.3
<b>Per share data (Rs)</b>				
EPS	56.3	73.4	80.0	101.4
DPS	12.7	12.7	12.7	12.7
BVPS	293.2	351.3	416.1	502.1
<b>Growth (%)</b>				
Net Sales	33.2	17.1	18.4	20.0
EBITDA	101.1	25.1	21.8	26.9
Net profit	71.9	30.4	9.0	26.7
<b>Operating Ratios</b>				
EBITDA Margin (%)	17.0	18.2	18.7	19.7
EBIT Margin (%)	15.0	15.6	16.1	17.3
PAT Margin (%)	13.5	15.0	13.8	14.6
<b>Return Ratios (%)</b>				
RoE	20.7	22.8	20.8	22.1
RoCE	21.1	22.9	23.5	25.2
<b>Turnover Ratios (x)</b>				
Net Sales/GFA	3.3	3.1	2.9	3.0

#### Rating Criteria

Large Cap.	Return	Mid/Small Cap.	Return
<b>Buy</b>	More than equal to 10%	<b>Buy</b>	More than equal to 15%
<b>Hold</b>	Upside or downside is less than 10%	<b>Accumulate*</b>	Upside between 10% & 15%
<b>Reduce</b>	Less than equal to -10%	<b>Hold</b>	Between 0% & 10%
		<b>Reduce/sell</b>	Less than 0%

\* To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.

\* Alkem is a Large-cap company

#### Disclaimer:

The SEBI registration number is INH200000394.

The analyst for this report certifies that all the views expressed in this report accurately reflect his / her personal views about the subject company or companies, and its / their securities. No part of his / her compensation was / is / will be, directly / indirectly related to specific recommendations or views expressed in this report.

This material is for the personal information of the authorized recipient, and no action is solicited on the basis of this. It is not to be construed as an offer to sell, or the solicitation of an offer to buy any security, in any jurisdiction, where such an offer or solicitation would be illegal.

We have reviewed the report, and in so far as it includes current or historical information, it is believed to be reliable, though its accuracy or completeness cannot be guaranteed. Neither Wealth India Financial Services Pvt. Ltd., nor any person connected with it, accepts any liability arising from the use of this document. The recipients of this material should rely on their own investigations and take their own professional advice. Price and value of the investments referred to in this material may go up or down. Past performance is not a guide for future performance.

We and our affiliates, officers, directors, and employees worldwide:

1. Do not have any financial interest in the subject company / companies in this report;
2. Do not have any actual / beneficial ownership of one per cent or more in the company / companies mentioned in this document, or in its securities at the end of the month immediately preceding the date of publication of the research report, or the date of public appearance;
3. Do not have any other material conflict of interest at the time of publication of the research report, or at the time of public appearance;
4. Have not received any compensation from the subject company / companies in the past 12 months;
5. Have not managed or co-managed the public offering of securities for the subject company / companies in the past 12 months;
6. Have not received any compensation for investment banking, or merchant banking, or brokerage services from the subject company / companies in the past 12 months;
7. Have not served as an officer, director, or employee of the subject company;
8. Have not been engaged in market making activity for the subject company;

This document is not for public distribution. It has been furnished to you solely for your information, and must not be reproduced or redistributed to any other person.

#### Contact Us:

#### Funds India

Uttam Building, Third Floor |  
No. 38 & 39 | Whites Road |  
Royapettah | Chennai – 600014 |

T: +91 7667 166 166

Email: [contact@fundsindia.com](mailto:contact@fundsindia.com)

## Dion's Disclosure and Disclaimer

I, Abhishek Kumar Das, employee of Dion Global Solutions Limited (Dion) is engaged in preparation of this report and hereby certify that all the views expressed in this research report (report) reflect my personal views about any or all of the subject issuer or securities.

### Disclaimer

This report has been prepared by Dion and the report & its contents are the exclusive property of the Dion and the client cannot tamper with the report or its contents in any manner and the said report, shall in no case, be further distributed to any third party for commercial use, with or without consideration.

Recipient shall not further distribute the report to a third party for a commercial consideration as this report is being furnished to the recipient solely for the purpose of information.

Dion has taken steps to ensure that facts in this report are based on reliable information but cannot testify, nor make any representation or warranty, express or implied, to the accuracy, contents or data contained within this report. It is hereby confirmed that wherever Dion has employed a rating system in this report, the rating system has been clearly defined including the time horizon and benchmarks on which the rating is based.

Descriptions of any company or companies or their securities mentioned herein are not intended to be complete and this report is not, and should not be construed as an offer or solicitation of an offer, to buy or sell any securities or other financial instruments. Dion has not taken any steps to ensure that the securities referred to in this report are suitable for any particular investor. This report is not to be relied upon in substitution for the exercise of independent judgment. Opinions or estimates expressed are current opinions as of the original publication date appearing on this report and the information, including the opinions and estimates contained herein, are subject to change without notice. Dion is under no duty to update this report from time to time.

Dion or its associates including employees engaged in preparation of this report and its directors do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of securities, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc.

The investments or services contained or referred to in this report may not be suitable for all equally and it is recommended that an independent investment advisor be consulted. In addition, nothing in this report constitutes investment, legal, accounting or tax advice or a representation that any investment or strategy is suitable or appropriate to individual circumstances or otherwise constitutes a personal recommendation of Dion.

### REGULATORY DISCLOSURES:

Dion is engaged in the business of developing software solutions for the global financial services industry across the entire transaction lifecycle and inter-alia provides research and information services essential for business intelligence to global companies and financial institutions. Dion is listed on BSE Limited (BSE) and is also registered under the SEBI (Research Analyst) Regulations, 2014 (SEBI Regulations) as a Research Analyst vide Registration No. INH100002771. Dion's activities were neither suspended nor has it defaulted with requirements under the Listing Agreement and / or SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 with the BSE in the last five years. Dion has not been debarred from doing business by BSE / SEBI or any other authority.

In the context of the SEBI Regulations, we affirm that we are a SEBI registered Research Analyst and in the course of our business, we issue research reports /research analysis etc that are prepared by our Research Analysts. We also affirm and undertake that no disciplinary action has been taken against us or our Analysts in connection with our business activities.

In compliance with the above mentioned SEBI Regulations, the following additional disclosures are also provided which may be considered by the reader before making an investment decision:



#### 1. Disclosures regarding Ownership

Dion confirms that:

- (i) Dion/its associates have no financial interest or any other material conflict in relation to the subject company (ies) covered herein at the time of publication of this report.
- (ii) It/its associates have no actual / beneficial ownership of 1% or more securities of the subject company (ies) covered herein at the end of the month immediately preceding the date of publication of this report.

Further, the Research Analyst confirms that:

- (i) He, his associates and his relatives have no financial interest in the subject company (ies) covered herein, and they have no other material conflict in the subject company at the time of publication of this report.
- (ii) he, his associates and his relatives have no actual/beneficial ownership of 1% or more securities of the subject company (ies) covered herein at the end of the month immediately preceding the date of publication of this report.

#### 2. Disclosures regarding Compensation:

During the past 12 months, Dion or its Associates:

- (a) Have not managed or co-managed public offering of securities for the subject company
- (b) Have not received any compensation for investment banking or merchant banking or brokerage services from the subject company
- (c) Have not received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject.
- (d) Have not received any compensation or other benefits from the subject company or third party in connection with this report

#### 3. Disclosure regarding the Research Analyst's connection with the subject company:

It is affirmed that I, Abhishek Kumar Das employed as Research Analyst by Dion and engaged in the preparation of this report have not served as an officer, director or employee of the subject company

#### 4. Disclosure regarding Market Making activity:

Neither Dion /its Research Analysts have engaged in market making activities for the subject company.

Copyright in this report vests exclusively with Dion.