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Q3FY21 result review
and earnings revision

Pharmaceuticals

Target price: Rs443

EBITDA revision

(%)	FY21E	FY22E	FY23E
Sales	(2.8)	(3.6)	(2.6)
EBITDA	(9.5)	(11.1)	(12.0)

Target price revision

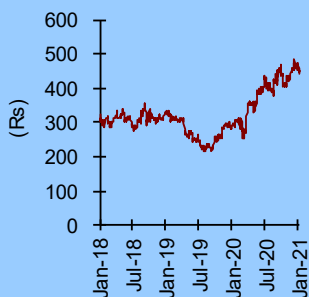
Rs443 from Rs490

Shareholding pattern

	Jun '20	Sep '20	Dec '20
Promoters	60.7	60.7	60.7
Institutional investors	23.1	23.0	23.7
MFs and other	4.7	3.9	3.1
FIs/Insurance	1.8	1.7	2.3
FIIIs	16.6	17.4	18.3
Others	16.2	16.3	15.6

Source: BSE India

Price chart



Research Analysts:

Vinay Bafna

vinay.bafna@icicisecurities.com
+91 22 6637 7339

Sriraam Rathi

sriraam.rathi@icicisecurities.com
+91 22 6637 7574

INDIA

Biocon Limited

ADD

Maintained

Rs394

Slow recovery in biosimilars

Biocon Limited (Biocon) reported lower than estimated Q3FY21 performance in biosimilars and generics segment. Consolidated revenues grew 7.8% to Rs18.5bn (I-Sec: Rs19.5bn), adjusted EBITDA margin was down 430bps to 21.6% (I-Sec: 25.4%) and adjusted PAT declined 16.9% to Rs1.7bn (I-Sec: Rs2.4bn). Lower margin is attributed to higher R&D expenses and employee costs. Delay in new launches and recovery in the environment would suppress margins in the near term but are expected to improve over medium term as the market normalises from impact of COVID-19. Dr Christiane Hamacher, has stepped down as the MD of Biocon Biologics and will be succeeded by Dr Arun Chandavarkar. Reiterate ADD with a revised target price of Rs443/share (earlier: Rs490/share).

- ▶ **Research steady while generics and biosimilars disappoint:** Research services grew 12.6% YoY with steady performance across its business segments. Company added a new project from 3DC that will support growth over medium term. Generics declined 2.6% YoY (-6.4% QoQ) to Rs5.6bn due to inventory correction of API products in the channel which were high in the distressed environment. Biosimilars segment grew 11.0% YoY during the quarter supported by steady market share in *Ogiviri* and *Fulphila* in the US and sales from the recently launched *Semglee* in US market. However, growth has been lower than expected as the company faced operational challenges due to lockdowns, delay in acquiring new tenders and reduced footfalls in hospital services and critical care due to the pandemic.
- ▶ **Higher R&D and staff costs restrict margin:** Company reported an improvement of 170bps in gross margin with improving business mix and higher contribution from biosimilar segment. However, staff and R&D expense jumped 23% and 31% respectively on a YoY basis. This sharp jump in costs is related to higher investment towards the biosimilars and generics pipeline and has hit EBITDA margin, which dropped 430bps YoY (-80bps QoQ) to 21.6%. PBT margins for biosimilars and generics segments declined to 14.4% and 9.6% respectively. Delay in recovery and new launches would suppress margins in the near term but are expected to improve over medium term as the market normalises from impact of COVID-19.
- ▶ **Outlook:** We expect revenue CAGR of 19.3% over FY20-FY23E resulting in EBITDA margin expansion of 450bps (with rising contribution from the high-margin biosimilars segment) and earnings CAGR of 34.2% over FY20E-FY23E. This would help generate healthy FCF of ~Rs11bn over FY21E-FY23E and improve return ratios.
- ▶ **Valuation and risks:** We reduce revenue and EBITDA estimates by 2-4% and 9-12% respectively over FY21E-FY23E to account for delay in new product launches and higher expenses towards R&D and personnel. Maintain **ADD** with a revised SoTP-based target price of Rs443/share (earlier: Rs490/share) **Key downside risks:** adverse regulation, delay in product launch, and higher competition in products.

Market Cap	Rs85bn/US\$1.2bn	Year to Mar	FY20	FY21E	FY22E	FY23E
Reuters/Bloomberg	BION.BO/BIOS IN	Revenue (Rs mn)	63,672	72,618	89,355	108,176
Shares Outstanding (mn)	51.0	Net Income (Rs mn)	6,986	6,981	11,508	16,877
52-week Range (Rs)	1806/864	EPS (Rs)	5.8	5.8	9.6	14.1
Free Float (%)	39.3	% Chg YoY	(6.2)	(0.1)	64.9	46.7
FII (%)	18.3	P/E (x)	67.7	67.7	41.1	28.0
Daily Volume (USD/'000)	8,784	CEPS (Rs)	10.4	11.7	16.0	21.3
Absolute Return 3m (%)	(7.1)	EV/E (x)	30.5	28.3	20.5	15.1
Absolute Return 12m (%)	23.2	Dividend Yield (%)	0.1	0.1	0.1	0.1
Sensex Return 3m (%)	20.7	RoCE (%)	7.3	6.3	9.6	13.1
Sensex Return 12m (%)	20.4	RoE (%)	10.9	9.9	14.6	18.3

Please refer to important disclosures at the end of this report

Q3FY21 result and concall highlights

Net revenues grew 7.8% YoY to Rs18.5bn supported by research and biosimilars business segments.

- Dr Christiane Hamacher, has stepped down as the MD of Biocon Biologics, effective 20th Jan'21, due to personal differences with Ms Kiran Mazumdar Shaw who will now assume the position of Executive Chairperson of Biocon Biologics. Dr Arun Chandavarkar, member of the board of Biocon Biologics will assume the role of MD for a period of upto two years.
- **Generics** declined 2.5% YoY to Rs5.6bn in Q3FY21. The decline was due to fall in demand for API products with inventory correction which were elevated in the distressed environment. Demand from newer markets was delayed since plant inspections owing to travel restrictions. Few product approvals in US were also delayed since the regulator could not inspect the plants. However, the company launched Tacrolimus capsules in US towards the end of the quarter. Company received a major CRL on *Copaxone* from USFDA to which it will respond in the coming months.
- **Biosimilars** segment grew 11.0% YoY (+13.7% QoQ) to Rs7.7bn in Q3FY21. Growth in the segment was lower than expected as the company faced operational challenges in scaling up production due to lockdowns, delay in acquiring new tenders and reduced footfalls in hospitals services and critical care due to the pandemic. However, steady market share in *Ogiviri* and *Fulphila* in the US, coupled with launch of *Semglee* in US and other geographies, have supported growth. Biocon is also building momentum in MoW markets with new launches and entering new markets with its key biosimilars (*Trastuzumab*, *rh-Insulin* and *Insulin Glargine*). *Bevacizumab* approval in US has been delayed since its contingent on plant inspection. EMA's CHMP has recommended approval of *Insulin Aspart* to treat Type1 and Type2 diabetes. It is also under review by USFDA.

Management has stated that they will reassess the timeline to reach the sales target of **US\$1bn from biosimilars** due to slow ramp up in existing products and delay in launches of new products owing to the pandemic.

During the quarter Biocon biologics received funds from ADQ and Goldman Sachs. Overall, it has raised US\$330mn from four rounds of infusion over the last year with an approximate equity dilution of ~11%.

- **Novel biologics** is currently a loss-making segment without any revenue, but is incurring investment towards key projects (*Tregopil*, *Itolizumab* and *BVX-20*). *Itolizumab* has received restricted emergency use approval from DCGI in India for treating CRS in moderate to severe ARDS patients due to COVID-19. Company has enrolled >100 out of 300 patients for phase-IV trial.
- **Research services** revenue grew 12.6% YoY (12.5% QoQ) to Rs 5.8bn. This growth was driven by good performance in discovery services and dedicated centre segments. Syngene was able to expand its integrated drug discovery platform with four new projects from 3DC during the quarter.
- **Gross margin** improved 170bps YoY (+30bps QoQ) to 69.8% with higher contribution from the biosimilars segment. **EBITDA margin** declined 430bps YoY (-80bps QoQ) to 21.6% with higher R&D and employee expenses.
- **R&D** costs for Q3FY21 stood at 9.2% of sales driven by investment in the biosimilars pipeline. **Adjusted PAT** declined 16.9% YoY to Rs1.7bn.

Table 1: Q3FY21 performance*(Rs mn, year ending March 31)*

	Q3FY21	Q3FY20	YoY % Chg	Q2FY21	QoQ % Chg
Net Sales	18,510	17,168	7.8	17,448	6.1
EBITDA	3,995	4,442	(10.1)	3,914	2.1
Other income	271	326	(16.9)	105	158.1
PBIDT	4,266	4,768	(10.5)	4,019	6.1
Depreciation	1,863	1,440	29.4	1,777	4.8
Interest	48	177	(72.9)	65	(26.2)
Extra ordinary income/ (exp.)	-	-	-	-	-
PBT (before extraordinary)	2,355	3,151	(25.3)	2,177	8.2
Tax	489	848	(42.3)	223	119.3
Minority Interest	180	275	(34.5)	261	(31.0)
Reported PAT	1,686	2,028	(16.9)	1,693	(0.4)
Adjusted PAT	1,686	2,028	(16.9)	1,693	(0.4)
EBITDA margins (%)	21.6	25.9	(430)bps	22.4	(80)bps

Source: Company data, I-Sec research

Table 2: Sales breakup*(Rs mn, year ending March 31)*

Segment Revenue	Q3FY21	Q3FY20	YoY % Chg	Q2FY21	QoQ % Chg
Generics	5,607	5,759	(2.6)	5,988	(6.4)
Biosimilars	7,689	6,930	11.0	6,761	13.7
Novel biologics	-	-	-	-	-
Research Services	5,845	5,191	12.6	5,196	12.5
Less: Inter-segmental revenue	631	712	(11.4)	497	27.0
Net Sales	18,510	17,168	7.8	17,448	6.1

Source: Company data, I-Sec research

Table 3: EBIT breakup*(Rs mn, year ending March 31)*

Segment EBIT	Q3FY21	Q3FY20	YoY % Chg	Q2FY21	QoQ % Chg
Generics	541	909	(40.5)	747	(27.6)
Biosimilars	1,106	1,429	(22.6)	808	36.9
Novel biologics	(514)	(335)	-	(307)	-
Research Services	1,165	1,067	9.2	942	23.7

Source: Company data, I-Sec research

Revising sales and EBITDA estimates

For FY20-FY23E, we forecast net sales and EBITDA to increase at CAGRs of 19.3% and 26.1% respectively. We reduce revenue estimates by 2-4% over FY21E-FY23E to factor-in lower sales on account of delay in new products launches and reduce EBITDA estimates by 9-12% over FY21E-FY23E to account for higher expenses towards R&D and personnel.

Table 4: Estimates revision

	FY21E	FY22E	FY23E
Total sales (Rs mn)			
Sales – new	72,618	89,355	108,176
Sales – old	74,699	92,669	111,059
Change (%)	(2.8)	(3.6)	(2.6)
EBITDA (Rs mn)			
EBITDA – new	17,499	24,099	32,109
EBITDA – old	19,340	27,119	36,504
Change (%)	(9.5)	(11.1)	(12.0)

Source: I-Sec research

Valuations

We expect Biocon to witness an earnings CAGR of 34.2% over FY20-FY23E driven by revenue CAGR of 19.3% and EBITDA margin expansion to 29.7% in FY23E from 25.2% in FY20. Return ratios (RoE and RoCE) would improve with margin expansion led by strong growth.

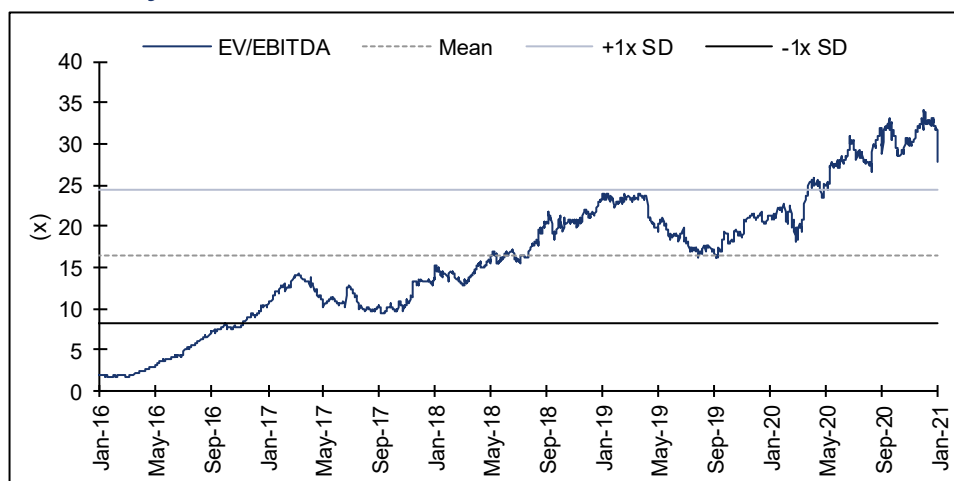
The stock currently trades at valuations of 41.1x FY22E and 28.0x FY23E earnings and EV/EBITDA multiple of 20.5x FY22E and 15.1x FY23E. We believe the company is poised for growth, especially in the biosimilars segment, driven by market share gain in existing products and new launches in developed as well as emerging markets. Steady performance in other business segments with improving profitability would also contribute towards sustainable earnings growth over the next few years. Hence, we remain positive on the long-term outlook of the company. We reiterate our **ADD** rating with a revised target price of Rs443/share (earlier: Rs490/share) based on SoTP valuation implying an EV/EBITDA of 16.9x in FY23E.

Table 5: Sum of the parts (SoTP) valuation

Segments	Rs mn	(x)	Biocon's stake	Value (Rs mn)
Generics	6,208	9	100%	55,868
Biosimilars	18,051	18	90%	292,076
Novel biologics	(1,000)	-	100%	-
Research Services (Syngene)	8,850	30	71%	187,690
Total EV				535,633
Less: Net Debt				395
Minority Interest (ex-Syngene)				4,077
Implied M-Cap				531,161
Value per share (Rs)				443

Source: I-Sec research

Chart 1: 1-year forward EV/EBITDA



Source: Company data, I-Sec research

Financial summary (consolidated)

Table 6: Profit & loss statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Total Net Revenue	63,672	72,618	89,355	108,176
YoY Growth%	15.5	14.1	23.0	21.1
Total Op. Exp.	47,641	55,119	65,256	76,066
EBITDA	16,031	17,499	24,099	32,109
Margins %	25.2	24.1	27.0	29.7
YoY Growth%	15.0	9.2	37.7	33.2
Depreciation	5,522	7,085	7,716	8,691
EBIT	10,509	10,415	16,383	23,418
Other Income	1,325	848	907	968
Interest	649	291	264	184
EO Items	675	-	-	-
PBT	11,860	10,973	17,025	24,203
Tax	3,151	2,765	4,290	6,099
Tax Rate (%)	26.6	25.2	25.2	25.2
Minority Interest	1,227	1,227	1,227	1,227
Reported PAT	7,482	6,981	11,508	16,877
Adj. PAT	6,986	6,981	11,508	16,877
Net Margins (%)	11.0	9.6	12.9	15.6

Source: Company data, I-Sec research

Table 7: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Paid-up Capital	6,000	6,000	6,000	6,000
Reserves & Surplus	61,058	67,409	78,286	94,533
Total Equity	67,058	73,409	84,286	100,533
Minority Interest	6,773	8,000	9,227	10,454
Total Debt	27,153	27,153	22,153	12,153
Deferred Liabilities	(3,382)	(3,382)	(3,382)	(3,382)
Capital Employed	97,602	105,180	112,284	119,758
Current Liabilities	43,156	46,942	54,799	63,480
Total Liabilities	140,758	152,122	167,084	183,238
Net Fixed Assets	81,813	94,728	102,012	108,321
Investments	943	943	943	943
Inventory	14,359	16,613	19,668	22,926
Debtors	12,237	13,956	17,173	20,790
Other Current Assets	12,844	13,981	16,108	18,500
Cash and Equivalents	18,562	11,900	11,180	11,758
Total Cur. Assets	58,002	56,450	64,129	73,974
Total Assets	140,758	152,122	167,084	183,238

Source: Company data, I-Sec research

Table 8: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
PBT (Adj. for Extraordinary)	11,860	10,973	17,025	24,203
Depreciation	5,522	7,085	7,716	8,691
Net Chg in WC	1,905	(2,829)	(3,358)	(3,754)
Taxes	(3,441)	(2,765)	(4,290)	(6,099)
Others	(3,664)	1,505	2,816	3,167
CFO	12,182	13,968	19,909	26,208
Capex	(18,294)	(20,000)	(15,000)	(15,000)
Net Investments made	1,744	-	-	-
Others	961	-	-	-
CFI	(15,589)	(20,000)	(15,000)	(15,000)
Change in Share capital	5,388	-	-	-
Change in Debts	186	-	(5,000)	(10,000)
Div. & Div Tax	(701)	(630)	(630)	(630)
Others	(2,052)	-	-	-
CFF	2,821	(630)	(5,630)	(10,630)
Total Cash Generated	(586)	(6,662)	(721)	578
Cash Opening Balance	10,572	9,986	3,324	2,604
Cash Closing Balance	9,986	3,324	2,604	3,182

Source: Company data, I-Sec research

Table 9: Key ratios

(Year ending March 31)

	FY20	FY21E	FY22E	FY23E
Adj EPS	5.8	5.8	9.6	14.1
YoY Growth%	(6.2)	(0.1)	64.9	46.7
Cash EPS	10.4	11.7	16.0	21.3
EBITDA (%)	25.2	24.1	27.0	29.7
NPM (%)	11.0	9.6	12.9	15.6
Net Debt to Equity (x)	0.1	0.2	0.1	0.0
P/E (x)	67.7	67.7	41.1	28.0
EV/EBITDA (x)	30.5	28.3	20.5	15.1
P/BV (x)	7.1	6.4	5.6	4.7
EV/Sales (x)	7.7	6.8	5.5	4.5
RoCE (%)	7.3	6.3	9.6	13.1
RoE (%)	10.9	9.9	14.6	18.3
RoIC (%)	8.9	7.2	10.6	14.4
Book Value (Rs)	55.9	61.2	70.2	83.8
DPS (Rs)	0.6	0.5	0.5	0.5
Dividend Payout (%)	0.1	0.1	0.1	0.0
Div Yield (%)	0.1	0.1	0.1	0.1
Asset Turnover Ratio	0.9	0.8	0.9	1.0
Avg Collection days	83	75	78	78
Avg Inventory days	95	103	101	102

Source: Company data, I-Sec research

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