

Emerging affordable biosimilars player in developed markets, insulins to be game changer



Biocon Q2FY22 results were better than estimates. While revenues were 6% below estimates, profitability improved due to higher gross margins. By segment, biosimilars (+10% yoy) and research services (+17% yoy). Generics -11% yoy on high base and +9% sequentially. We believe there are growth triggers like interchangeable glargine launch with 1 year exclusivity in biosimilars, Everolimus launch and market share gains in Tacrolimus for generics and robust demand for research services with the opening up of US and Europe.

- Sales came in at Rs 18404 mn (+5% yoy/+5% qoq)
- EBITDA (ex OI) came in at Rs 4458 mn (+14% yoy/ +15% qoq)
- EBITDA margins were at 24.2% (+180 bps yoy/+210 bps qoq), higher than our estimate of 23.7%.
- PAT (excl. exceptional) came in at Rs 2084 mn (+23% yoy/+147% qoq)
- EPS for the quarter was at Rs 1.74.
- Exceptional expense of Rs 701 mn due to reversal of export incentives for FY20.

Key Developments

- **Sales and sales growth by segments were**
 - Biosimilars Rs 7425 mn (+10% yoy/ -2% qoq)**
 - Generics Rs 5300 mn (-11% yoy/+9% qoq)**
 - Research Services (Syngene Rs 6102 mn +17% yoy/+3% qoq).**
- **EBIT margins by segment**
 - Biosimilars (+10% yoy/ -2% qoq)**
 - Generics Rs 5300 mn (-11% yoy/+9% qoq)**
 - Research Services (Syngene Rs 6102 mn +17% yoy/+3% qoq).**

Y/E Mar (Rs mn)	FY19	FY20	FY21	FY22E	FY23E
Net sales	55,144	63,005	71,212	78,977	1,06,682
EBITDA	13,937	15,364	16,680	19,286	30,244
Adjusted net profit	7,107	6,140	7,530	7,557	15,819
Free cash flow	(1,801)	(6,084)	(2,633)	(2,302)	9,675
EPS (Rs)	11.8	5.1	6.3	6.3	13.2
growth (%)	90.8	(13.6)	22.6	0.4	109.3
P/E (x)	27.1	62.7	51.2	51.0	24.4
P/B (x)	3.2	5.3	5.1	4.6	3.9
EV/EBITDA (x)	15.1	26.9	24.8	21.0	13.4
D/E	0.5	0.4	0.6	0.5	0.4
RoC (%)	10.4	7.7	8.8	9.1	17.7
RoE (%)	13.2	10.6	12.2	12.9	18.5
Dividend yield (%)	1.6	0	0	0	1.6

Source: Company

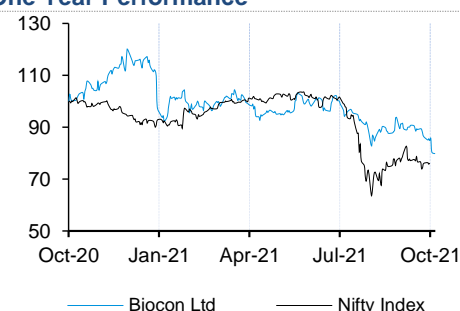
Rating	TP (Rs)	Up/Dn (%)
BUY	400	24

Market data

Current price	Rs	321
Market Cap (Rs.Bn)	(Rs Bn)	5,150
Market Cap (US\$ Mn)	(US\$ Mn)	68,768
Face Value	Rs	5
52 Weeks High/Low	Rs	488 / 315
Average Daily Volume	('000)	7754
BSE Code		532523
Bloomberg		BIOS.IN

Source: Bloomberg

One Year Performance



Source: Bloomberg

% Shareholding	Sep-21	Jun-21
Promoters	66.64	66.64
Public	38.64	38.45
Others	0.72	0.91
Total	100	100

Source: Bloomberg

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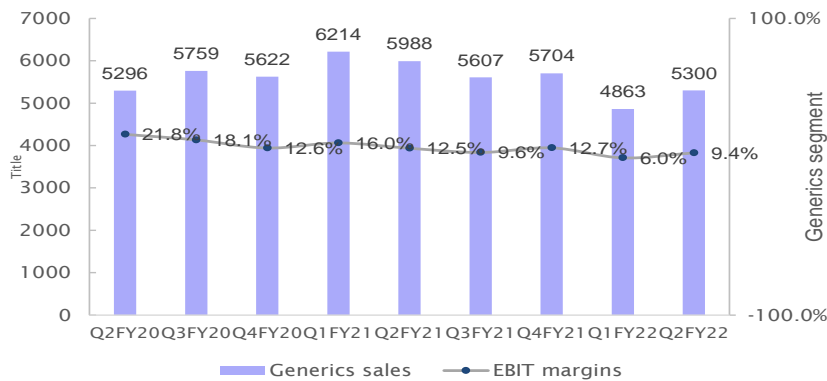
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Conference Call Highlights

A. Generics

1. Generics sales de-grew 12% on high base, price erosion in statins in the US and slower ramp up of demand for APIs.
2. The company expects ramp up in market share for Tacrolimus over the next few quarters.
3. In October, Biocon launched Everolimus which has 180 days exclusivity. with a day 1 launch in the 10 mg segment. Biocon will share exclusivity for the product with Breckinridge (+Natco). The launch will benefit the generics segment in terms of sales growth as well as profitability.
4. The USFDA conducted a virtual audit of its formulations facility at Bengaluru, as a pre-approval inspection for the company's ANDAs. The report is awaited.
5. Biocon's greenfield immunosuppressants API facility at Hyderabad will be commissioned in H2FY22, with qualification and certification in FY23.

Exhibit 1: Price erosion hurts Generics profitability

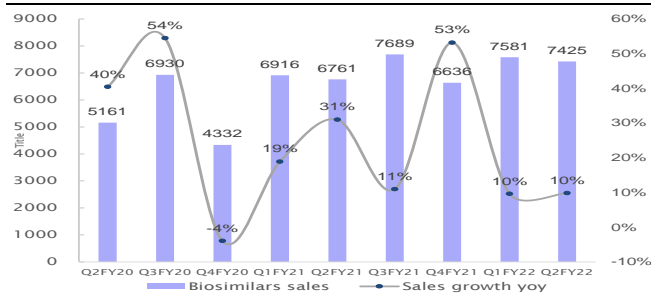


Source: Company, SSL

B. Biosimilars

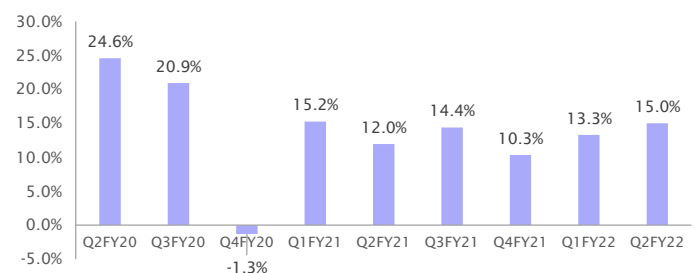
1. Biosimilars sales +10% yoy to Rs 7425 mn
2. The company aims for double digit market share for its biosimilars FULPHILA and OGIVRI in the US.
3. Launched Bevacizumab in new markets of Croatia, Germany, Czech Republic and Slovakia in Europe.
4. During the quarter, biosimilar sales between developed and MOW markets were at 46:54. The higher contribution from developed markets (40% in Q1FY22) improved EBIT margins for the segment sequentially.
5. Received USFDA approval for SEMGLEE with interchangeability, with an inclusion in Express Scripts formulary as a preferred brand in Glargine. Express Scripts has replaced Lantus with SEMGLEE and interchangeable insulin Glargine in its formulary. Express Scripts is the second largest PBM in the US, covering 28 mn lives.
6. The supplies for SEMGLEE and interchangeable insulin Glargine will commence Jan'22, with exclusivity for 1 year (CY2022).
7. Glargine currently has a market size of 120 mn pens, with SEMGLEE priced at \$30-35 Vs Lantus at \$65-68 per pen. Affordable insulin will enable savings in healthcare costs.
8. Received approval for Insulin ASPART from Canada.

Exhibit 2: Slower sales growth



Source: Company, SSL

Exhibit 3: Profitability impacted due to Covid19

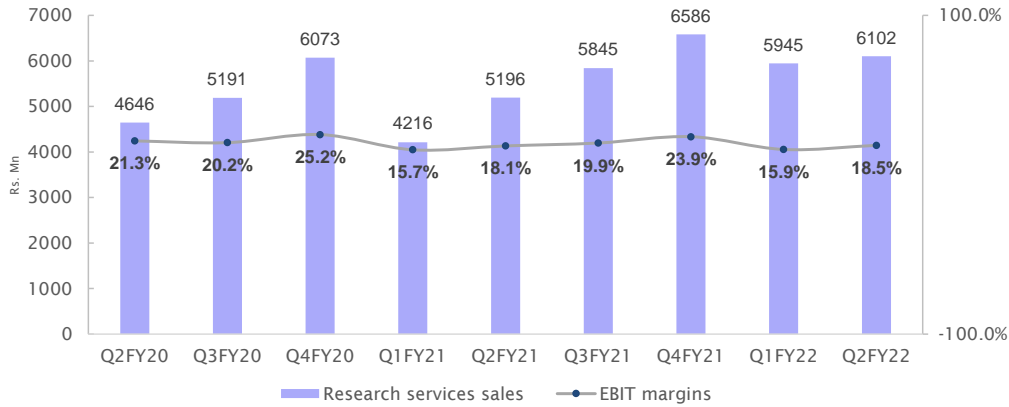


Source: Company, SSL

C. Research Services (Syngene)

9. Syngene revenues +17% to Rs 6102 mn. CC growth at 19%.
10. The revenue growth was across dedicated centres, discovery services & development & manufacturing.
11. The management expects USFDA approval for Mangalore API plant by H1FY24. The costs towards the facility will not be margin dilutive.
12. In Biologics, Syngene is working on the pathway for USFDA approval for its mammalian facility. The microbial facility has been commissioned recently and will update status in due course.

Exhibit 4: Profitability improves sequentially with better sales mix



Source: Company, SSL

D. Novel Biologics

1. Equillum to initiate phase III pivotal study for the use of Itolizumab in the treatment of Acute Graft Vs Host Disease in Q4CY2021.

Quarterly Financials

Particulars	Q2FY22	Q1FY22	Q2FY21	Q1FY21	% yoy	% qoq	FY21	FY20	% yoy
Net Sales	18404	17606	17448	16938	5%	5%	71212	63005	13%
<i>Biosimilars</i>	7425	7581	6761	6916	10%	-2%	28002	23151	21%
<i>Generics</i>	5300	4863	5988	6214	-11%	9%	23513	22070	7%
<i>Research Services</i>	6102	5945	5196	4216	17%	3%	21843	20119	9%
Raw Material Consumed	(5651)	(6121)	(5314)	(5628)			(22085)	(20522)	
Employee Expenses	(4788)	(4360)	(4319)	(3937)			(17410)	(14588)	
Research & Development Exps	(1460)	(1200)	(1480)	(1070)			(4765)	(4390)	9%
Other Expenses	(2047)	(2032)	(2421)	(2170)			(10272)	(8141)	
Total Exp	(13946)	(13713)	(13534)	(12805)	3%	2%	(54532)	(47641)	14%
PBDIT	4458	3893	3914	4133	14%	15%	16680	15364	9%
Depreciation	(2015)	(1948)	(1777)	(1668)			(7151)	(5522)	
<i>EBIT</i>	2443	1945	2137	2465			9529	9842	-3%
<i>EBIT margins</i>	13.3%	11.0%	12.2%	14.6%			13.4%	15.6%	
Other Income	1049	472	155	183			2545	1614	
Interest	(225)	(199)	(65)	(125)			(577)	(649)	
Profit before tax	3267	2218	2227	2523	47%	47%	11497	10807	6%
Tax (incl. on exceptional income)	(463)	(573)	(223)	(809)			(2215)	(3151)	
Profit After tax	2804	1645	2004	1714	40%	70%	9282	7656	
<i>NPM (%)</i>	15.2%	9.3%	11.5%	10.1%			13.0%	12.2%	
Less: Minority interest	(214)	(240)	(261)	(184)			(1057)	(1227)	
Share of Profit	(506)	(561)	(50)	(36)			(695)	(289)	
Adjusted PAT	2084	844	1693	1494	23%	147%	7530	6140	23%
Extraordinary Items after tax	(701)	0	0	0			126	675	
Reported PAT	1383	844	1693	1494	-44%	-67%	7656	6815	12%
Number of shares	1200	1200	1200	1200			1200	1200	
EPS without excep. Items	1.7	0.7	1.4	1.2			6.3	5.1	
EPS - Diluted (Rs)	1.2	0.7	1.4	1.2			6.4	5.7	

Research services and biosimilars drive revenue growth,

generics degrowth from price erosion

Other income higher due to profit on sale of investments

Healthy growth in adjusted PAT

Exceptional expenses due to reversal of export incentives in view of cap of Rs 50 mn.

Margin Analysis	Q1FY22	Q1FY22	Q2FY21	Q1FY21	+/- bps	+/- bps	FY21	FY20	% yoy
Gross margin	69.3%	65.2%	69.5%	66.8%	-154	-334	69.0%	67.4%	156
EBITDA margin	24.2%	22.1%	22.4%	24.4%	-229	-154	23.4%	24.4%	-96
PBT margin	17.8%	12.6%	12.8%	14.9%	-230	-1036	16.1%	17.2%	-101
PAT margin	7.5%	4.8%	9.7%	8.8%	-403	-895	10.8%	10.8%	-7

Valuation & Outlook

At Rs 321, Biocon trades at 24x FY23E EPS of Rs 13.5 and 12x EV/EBITDA. We have valued Biocon as weighted average (33:34:33) of 30x P/E, 15x EV/EBITDA and DCF and arrived at a **target price of Rs 400**.

In view of the interchangeable Glargine launch in US in CY2021 in biosimilars, Everolimus launch with exclusivity in generics and larger research service offerings (Syngene), in line with international CRO's and expected ramp up in the coming quarters, **we upgrade our rating from BUY on Dips to BUY**.

Financials

P&L (Rs mn)	FY19	FY20	FY21	FY22E	FY23E	Cash Flow St. (Rs. mn)	FY19	FY20	FY21	FY22E	FY23E
Net Sales	55,144	63,005	71,212	78,977	1,06,682	Net Profit	9,053	6,815	7,656	7,557	15,819
Raw materials	(18,966)	(20,522)	(22,085)	(24,483)	(33,071)	Add: Dep. & Amort.	4,478	5,522	7,151	7,773	8,589
Employee costs	(11,653)	(14,588)	(17,410)	(20,892)	(26,115)	Cash profits	13,531	12,337	14,807	15,330	24,408
Other Expenses	(7,688)	(8,141)	(10,272)	(9,655)	(12,069)	(Inc)/Dec in					
Research & Devt	(2,900)	(4,390)	(4,765)	(4,661)	(5,182)	-Sundry debtors	(2,279)	681	61	(1,362)	(4,749)
Cost of sales	(41,207)	(47,641)	(54,532)	(59,691)	(76,438)	-Inventories	(3,091)	(4,043)	(4,307)	(326)	(6,560)
Operating Profit	13,937	15,364	16,680	19,286	30,244	-Loans/advances	(1,475)	224	(5,908)	-	-
Depreciation	(4,478)	(5,522)	(7,151)	(7,773)	(8,589)	-Sundry creditors	1,930	1,268	1,888	597	5,520
PBIT	9,459	9,842	9,529	11,513	21,655	-Others	1,714	3,439	447	2,154	2,585
Other income	1,444	1,614	2,545	2,927	3,512	Change in WC	(3,201)	1,569	(7,819)	1,064	(3,203)
Interest	(709)	(649)	(577)	(597)	(608)	CF from Oper. activities	10,330	13,906	6,988	16,395	21,205
Profit before tax	10,194	10,807	11,497	13,842	24,559	CF from Inv. activities	(12,263)	(15,783)	(9,109)	(5,766)	(9,961)
Provision for tax	(2,123)	(3,151)	(2,215)	(3,045)	(6,140)	CF from Fin. activities	961	9,718	21,830	(11,477)	(11,065)
Profit after Tax	8,071	7,656	9,282	10,797	18,419	Cash generated/(utilisec)	(972)	7,841	19,709	(847)	180
Minority Interest	(973)	(1,227)	(1,057)	(1,000)	(1,100)	Cash at start of the year	13,395	10,572	15,346	20,154	17,389
Share of Profit	9	(289)	(695)	(2,240)	(1,500)	Cash at end of the year	10,572	15,346	20,154	17,389	15,186
Adjusted PAT	7,107	6,140	7,530	7,557	15,819	Ratios	FY19	FY20	FY21	FY22E	FY23E
Extraordinary Items	1,946	675	126	-	-	OPM	25.3	24.4	23.4	24.4	28.3
Reported PAT	9,053	6,815	7,656	7,557	15,819	NPM	16.0	10.5	10.4	9.2	14.4
Balance Sheet	FY19	FY20	FY21	FY22E	FY23E	Tax rate	(20.8)	(29.2)	(19.3)	(22.0)	(25.0)
Equity capital *	3,000	6,000	6,000	6,000	6,000	Growth Ratios (%)					
Reserves	57,980	66,418	70,269	77,826	93,645	Net Sales	33.5	14.3	13.0	10.9	35.1
Equity Dilution	-	5,360	-	-	-	Operating Profit	68.1	10.2	8.6	15.6	56.8
Net worth	60,980	72,418	76,269	83,826	99,645	PAT excl. EI	90.8	(13.6)	22.6	0.4	109.3
Def. Tax Liab.+Minority I	6,089	7,071	9,130	10,011	10,979	Per Share (Rs.)*					
Secured loans	15,256	12,222	29,616	23,816	23,857	Adj. Net Earnings (EPS)	11.8	5.1	6.3	6.3	13.2
Unsecured loans	2,612	6,676	5,942	2,276	2,277	Cash Earnings (CPS)	22.6	10.3	12.3	12.8	20.3
Current maturities	10,066	12,978	13,069	13,722	14,409	Dividend	5.0	-	-	-	5.0
Total debt	27,934	31,876	48,627	39,815	40,543	Book Value	101.6	60.3	63.6	69.9	83.0
Other liab	8,052	14,857	25,286	25,833	26,941	Free Cash Flow	(3.2)	(1.6)	(1.8)	8.9	9.4
CAPITAL EMPLOYED	1,03,055	1,26,222	1,59,312	1,59,484	1,78,108	Valuation Ratios					
Gross block	68,019	85,523	94,315	1,14,315	1,26,315	P/E(x)	27.1	62.7	51.2	51.0	24.4
Accumulated depreciatic	(26,069)	(31,591)	(38,742)	(46,515)	(55,105)	P/B(x)	3.2	5.3	5.1	4.6	3.9
Net block	42,527	53,932	55,573	67,800	71,210	EV/EBIDTA(x)	15.1	26.9	24.8	21.0	13.4
Capital WIP	12,869	15,765	22,535	10,000	10,000	EV/SALES (x)	3.8	6.6	5.8	5.1	3.8
Total fixed assets	55,396	69,697	78,108	77,800	81,210	Div. Yield(%)	1.6	-	-	-	1.6
Intangible Assets	8,303	10,691	12,000	12,000	12,000	FCF Yield(%)	(1.0)	(0.5)	(0.6)	2.8	2.9
Investments	10,118	9,661	19,519	23,064	35,825	Return Ratios (%)					
Other non current asset:	2,131	1,514	1,756	2,107	2,529	ROE	13.2	10.6	12.2	12.9	18.5
Right of use assets	-	1,283.0	1,533.0	1,533.0	1,533.0	ROCE	11.8	8.8	6.4	7.7	13.0
Assets for sale	-	-	522	522	522	ROIC	10.4	7.7	8.8	9.1	17.7
Inventories	10,316	14,359	18,666	18,992	25,552						
Sundry debtors	12,918	12,237	12,176	13,538	18,286						
Cash & bank	10,572	15,346	20,154	17,389	15,186						
Loans & advances	5,742	5,518	11,426	11,426	11,426						
Other current assets	1,488	3,395	3,638	4,002	4,402						
Sundry creditors	(11,983)	(13,251)	(15,139)	(15,736)	(21,257)						
Acceptances	(5,420)	(8,437)	(8,616)	(10,339)	(12,407)						
Provisions	(1,466)	(1,888)	(2,156)	(2,587)	(3,105)						
Working capital	27,107	33,376	45,874	42,981	45,011						
CAPITAL DEPLOYED	1,03,055	1,26,222	1,59,312	1,59,484	1,78,108						

* Increase in Equity on account of bonus issue in FY17 (2:1) and FY19 in the proportion of 1:1

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