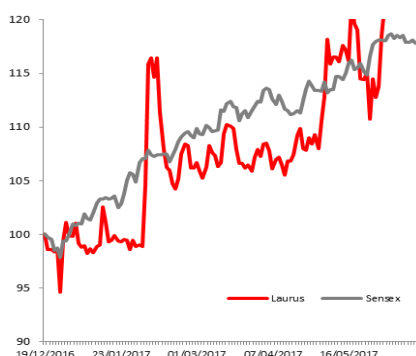



Initiating Coverage@ Dalal & Broacha
BUY

Current Price	627
Target Price	744
Upside/Downside	19%
52 Week Range	634/453

Key Share Data

Market Cap (Rs.bn)	66.3
Market Cap (US\$ mn)	1028.05
No of o/s shares (mn)	105.8
Face Value	10
Monthly Avg.vol (BSE+NSE) Nos'000	219
BSE Code	540222
NSE Code	LAURUSLABS
Bloomberg	LAURUS:IN

Price performance


% Shareholding	Mar-17	Dec-16
Promoters	30.64	30.64
FII	11.09	6.62
DII	41.44	41.01
Others	16.83	21.73
Total	100	100

Key Financials

Year	Sales	% Growth	EBIDTA	OPM (%)	PAT	% Growth	EPS	PE (x)	RoE (%)	RoCE (%)
FY16	17775.8	34%	3622.0	20.4%	1337.4	95%	12.65	7.4	17%	15%
FY17	19046.5	7%	4076.4	21.4%	1902.8	42%	17.99	34.8	14%	15%
FY18E	22916.3	20%	4958.8	21.6%	2502.2	32%	23.66	26.5	16%	17%
FY19E	29837.1	30%	6824.4	22.9%	3746.3	50%	35.42	17.7	20%	21%

Better API product mix, formulations foray to drive earnings growth

We are positive on the progress of Laurus Labs in view of the research capabilities of the promoters. The company has carved out a niche through high volume therapies of anti retrovirals (ARVs), Hepatitis C and Oncology. Laurus Labs has tied up with formulation manufacturers, in India and abroad for API supplies. Being an innovator of molecules in different therapies, we expect Laurus Labs to benefit from strategic tie-ups with partners. Further, the forward integration into formulations will help improve profitability. We also expect growth from custom synthesis with the commissioning of its plant for steroids and hormones in November'16. The resultant improvement in profitability due to better product mix in APIs and higher contribution from formulations and custom synthesis will lead to earnings growth. We initiate coverage on Laurus Labs and recommend investors to BUY the stock with a target price of Rs 744, indicating an upside of 19%.

Investment Argument
Promoters strength in research capabilities

Laurus Labs has a robust set of 4 promoters, who are well qualified and highly experienced professionals with rich experience in the pharmaceutical industry. Laurus has been promoted by Dr. Satyanarayana Chava, who has been determined as inventor in 103 patents approved and filed throughout the world.

Niche through research with focus on high volume therapies

Laurus Labs has strategically carved out a niche through product innovation in high volume therapeutic areas with an unmet need. The company is a leading supplier of APIs in anti retrovirals (ARVs) used for the treatment of HIV patients, hepatitis C (Hep C) and oncology. Being the innovator, Laurus Labs is well positioned to benefit as a game changer in the molecules of its interest.

Strategic tie ups, formulations, custom synthesis to augment growth

We expect Laurus Labs to benefit from its strategic tie up with formulation manufacturers. The commissioning of its formulations plant by Q4FY18 and increased custom synthesis is expected to augment growth with an improvement in profitability.

Revenues to grow at 19% CAGR, faster earnings growth due to better profitability

We expect revenues to grow at 19% CAGR to Rs 29 bn by FY19. EBITDA will grow at 24% CAGR to Rs 6.8 bn, with EBITDA margins improving to 22.9% by FY19. We expect PAT to grow 41% CAGR to Rs 3.75 bn.

Outlook and Valuation

We strongly believe investment in Laurus Labs will yield good returns in the long term. We expect earnings growth through a better product mix in APIs, foray into formulations and custom synthesis. Further, the company's plant has been cleared by USFDA leaving no pending regulatory issues. At Rs 627, Laurus Labs trades at 18x FY19E EPS of Rs 35.4. We recommend investors to BUY Laurus Labs for long term.

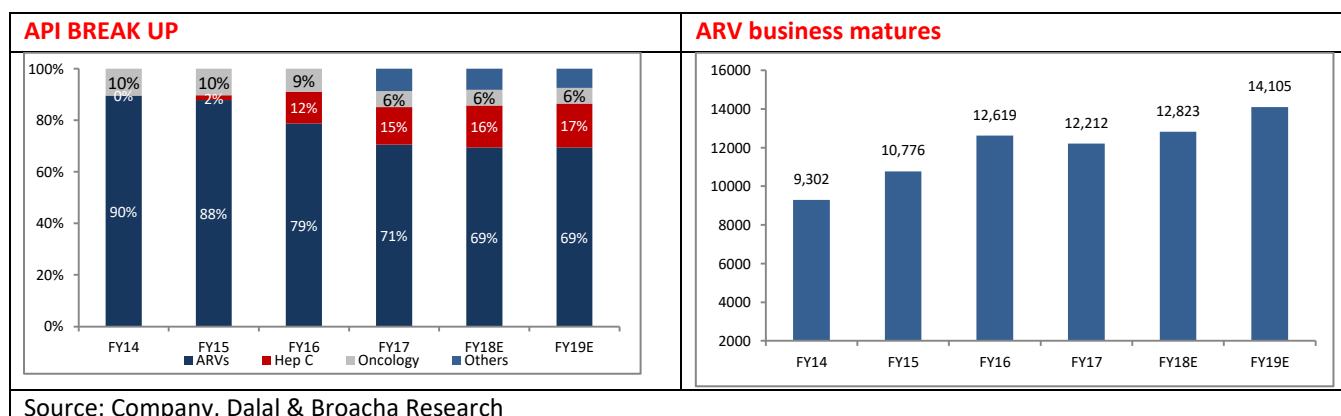
Investment Argument

Promoters' strength in research capabilities

Laurus Labs has a robust set of 4 promoters, who are well qualified and highly experienced professionals with rich experience in the pharmaceutical industry. Laurus has been promoted by Dr. Satyanarayana Chava, who has been determined as inventor in 103 patents approved and filed throughout the world. Dr. Raju Kalidindi is also one of the promoters of Laurus, who has been determined inventor in 11 patents granted or filed all over the world. Laurus has a team of 599 scientists, focussed on innovating different processes in order to make it cost effective and scalable. We believe the promoter's strength in research capabilities will help Laurus grow through innovations adding to its product basket.

Niche through research with focus on high volume therapies

Laurus Labs has strategically carved out a niche through product innovation in high volume therapeutic areas with an unmet need. The company is a leading supplier of APIs in anti retrovirals (ARVs) used for the treatment of HIV patients, hepatitis C (Hep C) and oncology. The World Health Organisation (WHO) expects the number of HIV patients to increase from 17 mn in 2015 to 23.5 mn by 2018. Similarly, the WHO estimates 175-180 mn patients to be infected with Hepatitis C globally, of which 12-18 mn patients are from India. We believe Laurus is well positioned as an innovator of cost effective molecules. The company's focus on high volume therapies has helped in scaling up the business. Being the innovator, Laurus Labs is well positioned to benefit as a game changer in the molecules of its interest.



ARVs grow to mature, presence in entire treatment range

Laurus Labs entered the ARVs business in FY10. The business scaled up to cover the entire range of treatment for HIV patients, namely Tenofovir Disoproxil Fumarate (TDF), Lamivudine (3TC), Emtricitabine (FTC) and Efavirenz (EFV). ARV revenues grew at 16% CAGR to Rs 12619 mn upto FY16. During FY17, ARV revenues were at Rs 12212 mn, indicating a 3% de-growth due to pricing pressure. However, in Q4FY17, the company commenced exports of ARVs to Europe. Laurus Labs also plans to launch newer second line of HIV treatment in the emerging markets. Going forward, we expect the ARVs business to grow by 5-10% to Rs 14575 mn by FY19.

Oncology poor performer, entry into Hepatitis C augurs Generics API growth

Upto FY16, the company's oncology portfolio grew at 14% CAGR to Rs 1413 mn. In FY17, the portfolio de-grew 24% to Rs 1073 mn, mainly due to pricing pressure in the therapy. While the ARVs portfolio matured, Laurus Labs launched its Hepatitis C API in FY15. The company then expanded its product range to cover the latest drugs namely Sofosbuvir, Daclatasvir and the combination of Ledipasvir and Sofosbuvir. Revenues from Hep C grew manifold from Rs 231 mn in FY15 to Rs 2509 mn by FY17.

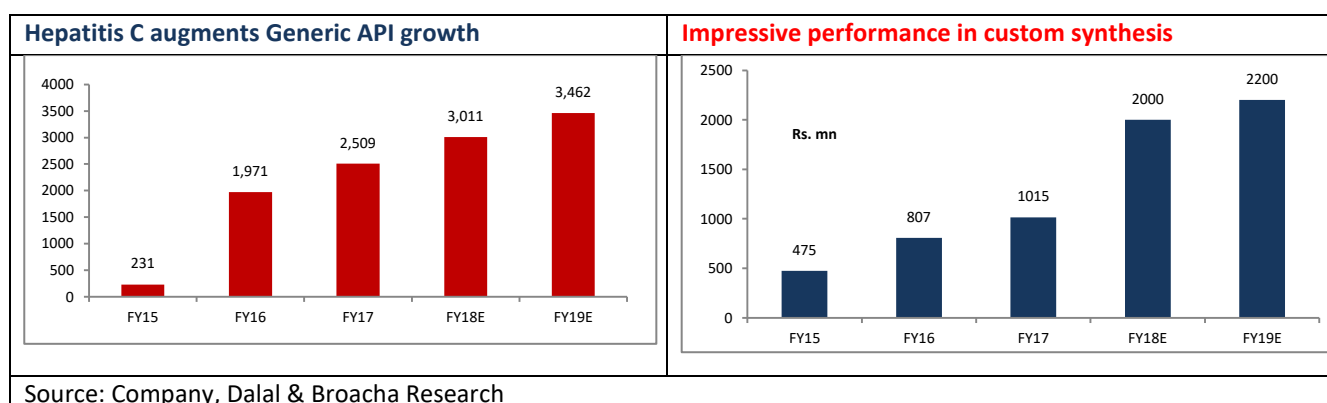
Strategic tie ups with formulation manufacturers boost performance

Apart from expanding the range of APIs in Hepatitis C, Laurus Labs entered into a long term license agreement with Gilead Sciences, Ireland to manufacture and sell Sofosbuvir, Ledipasvir and Velpatasvir within specified jurisdictions. The company also

entered into a tripartite and technology agreement with Bristol Myers Squibb and Medicines Patent Pool Foundation for the manufacture and sale of Daclatasvir in specified jurisdiction.

Laurus Labs also entered into a cost and profit sharing agreement with Natco Pharma for the supply of APIs for Hepatitis C formulations. Natco Pharma is the market leader in Hepatitis C with a market share of 38% in the Indian market. In January'17 Natco launched the first generic combination of Sofosbuvir and Velpatasvir in Nepal. Earlier this month, Natco launched the combination in India. Going forward, we expect revenues from Hepatitis C to grow at 19% CAGR to Rs 3462 mn by FY19.

We expect Generics API to grow at 11% CAGR to Rs 22507 mn, driven by growth in Hepatitis C, ARVs and entry into diabetes and proton pump inhibitors for lifestyle diseases.



Forward integration into formulations

With more than 90% of revenues from generics- APIs, Laurus Labs now plans to expand into formulations. The company is expanding its formulations capacity from 1 bn tablets to 5 bn tablets incurring capex of Rs 4 bn. The new facility is expected to be commissioned by December'17. Laurus Labs has entered into cost and profit sharing agreements with Dr. Reddy's, Natco Pharma and Citron Pharma LLC for supplying formulations in different therapeutic areas. The company has received the establishment inspection report (EIR) from the USFDA for the existing formulations facility and awaits approval from the World Health Organisation (WHO). We expect the generic formulations business to generate revenues from FY18 and scale up to contribute 9-10% of consolidated revenues by FY19. We expect Laurus Labs to benefit from the forward integration into formulations, resulting in better profitability.

Dedicated custom synthesis for Aspen, South Africa

Laurus Labs has tied up with Aspen Pharma, South Africa for a dedicated research centre and the manufacturing of hormones and steroids. The company commissioned a dedicated facility in November'16 for the manufacture of hormones and steroids. As per the agreement, Laurus Labs will supply the API to Aspen Pharma, who in turn will supply to Merck for formulations to the regulated markets.

The company also provides custom synthesis to global clients for new chemical entities (NCEs) which are in various stages of clinical trials. The business may throw up huge opportunities, which have not been factored into our estimates. We expect custom synthesis to grow at 40% CAGR to Rs 2200 mn by FY19, contributing ~10% of revenues.

Financial Outlook

Healthy revenue growth from all businesses

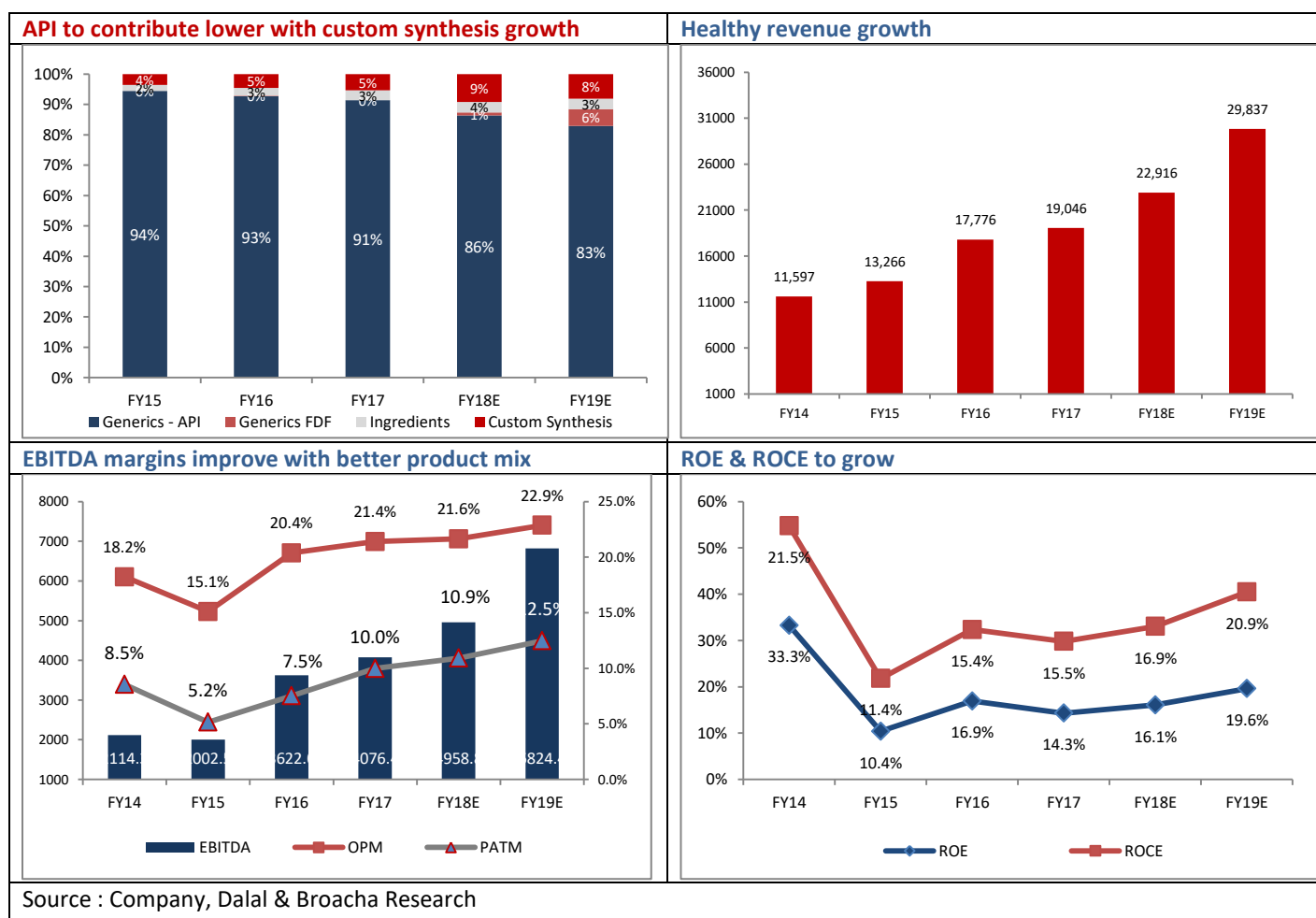
We expect revenues to grow at 19% CAGR to Rs 30 bn by FY19. Revenues will grow from Generic APIs, FDFs, custom synthesis as well as ingredients.

Better product mix improves profitability

The improved product mix in APIs due to a lower contribution of ARVs, lower contribution of APIs due to growth in revenues from custom synthesis and generic FDFs will lead to an expansion in EBITDA margin. We expect a 150 bps increase EBITDA margins by FY19.

Repayment of debt leads to faster earnings growth

Laurus Labs has repaid debt during FY17 resulting in lower interest costs. The lower interest costs will lead to a faster earnings growth.



Company Background

Laurus Labs has been promoted by Dr. Satyanarayana Chava, Dr. Raju Kalidindi, and Mr. V. V Ravikumar and Dr. Lakshmana Rao C V in 2006. The promoters are highly experienced in research & development with credits from the pharmaceutical industry. The management is also backed by an experienced second line, which augurs well for the company.

Laurus Labs has five manufacturing facilities at Visakhapatnam and state of the art research laboratories at Hyderabad. The company also has a kilo lab at Hyderabad.

Manufacturing facilities and its certifications

Of the five manufacturing facilities, three facilities are approved by the USFDA and WHO-Geneva. One of the facilities is certified by BfARM – Germany. All the facilities of the company are located in Andhra Pradesh.

Research & Development facilities

The research & development facility and the kilo lab of the company are USFDA certified.

Currently, Laurus Labs has 37 drug master files (DMFs), of which 30 have been commercialised.

Laurus Labs went public in December'16, with a fresh issue of equity shares and offer for sale from investors at Rs 428 per share. The company received Rs 3000 mn from the public issue, which has been utilised for the repayment of debt and financing capital expenditure.

In FY17, Laurus Labs earned revenues of Rs 19046 mn. 91% of the revenues were from Generic – APIs, 5% from custom synthesis and 3% from ingredients. Of the Generic APIs, 71% came from ARVs, 15% from Hepatitis C, 6% from oncology and 9% from other APIs.

Laurus Labs generates 85% of its revenues from exports (35% direct and 50% deemed exports), with the balance from India.

Valuation

We have valued Laurus Labs by the Price to Earnings method of valuation. We have applied a Price to earnings multiple of 21x FY19E EPS of Rs 35.4. At Rs 627, Laurus Labs trades at 18x FY19E EPS of Rs 35.4. We arrive at a target price of Rs 744 per share, indicating an upside of 19%.

Company	3/7/2017		EPS				P/E Multiple			
	CMP	MCAP	FY16	FY17	FY18E	FY19E	FY16	FY17	FY18E	FY19E
Divis Labs	670.1	48588	39.85	45.1	37.9	41.3	16.8	14.9	17.7	16.2
Granules India	139.6	30578	5.5	6.1	6.2	6.5	25.4	22.8	22.6	21.4
Laurus Labs	627	57283	12.6	18.0	23.7	35.4	49.6	34.8	26.5	17.7
Natco Pharma	1014.5	501061	8.9	24	27.7	33.9	114.0	42.3	36.6	29.9
Syngene	472	91310	11.11	14.37	15.63	20.87	56.4	32.9	30.2	22.6
AVERAGE								29.5	26.7	21.6

LAURUS LABS FINANCIALS

PROFIT & LOSS (Rs mn)	FY16	FY17	FY18E	FY19E	CASH FLOW	FY16	FY17	FY18E	FY19E
Revenue from Operations (Net)	17775.78	19046.47	22916.3	29837.05	Profit After Tax	1337.4	1902.8	2502.2	3746.3
Raw Material Costs	10081.6	9967.7	12031.1	15664.5	Add: Depreciation	864.1	1059.8	1106.8	1275.5
Gross Profit	7694.2	9078.8	10885.2	14172.6	Cash Profits	2201.4	2962.6	3609.0	5021.8
<i>Gross Margins</i>	43.3%	47.7%	47.5%	47.5%	(Increase)/ Decrease in:-				
Employee Benefits Expenses	1,885.2	2,462.3	2,954.8	3,545.7	Trade receivables	-1,597.9	-1,227.5	-1,230.2	-1,268.3
Other Manufacturing Expenses	757.4	795.3	874.8	918.5	Long Term Loans & Advances	1,185.6	-97.7	-37.7	-45.2
Research & Development Expenses	796.2	952.3	1,145.8	1,790.2	Short Term Loans & Advances	-268.0	-80.0	-100.4	-179.6
Operating and Selling Expenses	633.5	792.6	951.1	1,093.7	Other current assets	-268.0	-80.0	-100.4	-179.6
EBITDA	3622.0	4076.4	4958.8	6824.4	Inventories	-116.0	-219.5	-1,065.5	-1,729.1
Depreciation and Amortisation	864.1	1059.8	1106.8	1275.5	Trade payables	168.0	154.9	500.4	816.9
EBIT	2757.9	3016.5	3852.0	5548.8	Short term provisions	-15.5	24.7	20.6	36.8
Finance Expenses	1,111.1	999.0	799.4	726.7	Other current liabilities	-1,161.9	413.1	118.8	212.4
Other Income	43.6	334.4	133.8	120.4	Other Non Current Assets	-450.4	87.4	-50.3	-55.3
Profit Before Tax	1690.4	2352.0	3186.3	4942.5	Other Long Term Liabilities	-281.9	466.1	63.1	69.4
Tax Expense	349.0	438.6	669.1	1186.2	Long Term Provision	16.5	24.0	18.6	33.3
Share of results of associate	-4.02	-10.55	-15	-10	Working Capital change	-2,789.6	-534.6	-1,863.2	-2,288.3
Profit for the year	1337.4	1902.8	2502.2	3746.3	Net Cash generated from operations	979.0	2,711.9	1,996.6	3,078.5
					Net Cash from Investing activities	-2667.0	-3854.4	-1172.6	-2205.5
					Net Cash (used in)/ generated from financing activities	1,386.9	959.3	-667.5	-309.3
BALANCE SHEET					Net increase/(decrease) in cash and cash equivalents	-301.1	-183.1	156.5	563.6
Share Capital	157.7	1057.6	1057.6	1057.6					
Reserves & Surplus	7,744.2	12,246.9	14,501.7	17,938.6	Cash & Cash equivalents at the beginning of the year	588.9	287.7	104.6	261.1
Net Worth	7901.9	13304.5	15559.2	18996.2	Cash & Cash equivalents at the end of the year	287.7	104.7	261.1	824.7
Preference Shares	666.1	0.0	0.0	0.0					
Long term Borrowings	4,597.4	1,245.6	825.6	825.6	Ratios				
Short term Borrowings	4,814.2	6,441.7	6,441.7	6,441.7	OPM	20.4%	21.4%	21.6%	22.9%
TOTAL DEBT	9,411.6	7,687.3	7,267.3	7,267.3	NPM	7.5%	10.0%	10.9%	12.6%
Other Long-term liabilities	164.7	630.7	693.8	763.2	Tax rate	21%	19%	21%	24%
Deferred tax Liabilities (Net)	0.0	0.0	0.0	0.0					
CAPITAL EMPLOYED	18144.2	21622.5	23520.3	27026.7	Growth Ratios (%)				
Tangible assets - Gross	12,860.0	15,896.9	16,396.9	18,896.9	Net Sales	34%	7%	20%	30%
Acc. Depreciation	2,713.6	3,773.4	4,880.2	6,155.8	Operating Profit	81%	13%	22%	38%
Net Block - Tangibles	10,146.4	12,123.4	11,516.6	12,741.1	PAT	95%	42%	32%	50%
Net Block - Intangibles	63.9	78.5	82.5	86.6					
Capital Work in Progress	696.0	1432.6	2000.0	1000.0	Per Share (Rs.)				
Total Fixed Assets	10,906.3	13,634.5	13,599.1	13,827.7	Net Earnings (EPS) - Diluted	12.65	17.99	23.66	35.42
Goodwill	0.00	97.39	97.39	97.39	Cash Earnings (CPS) - Diluted	20.82	28.01	34.13	47.48
Non-current Investment	70.5	0.0	0.0	0.0	Number of shares	15.77	105.76	105.76	105.76
Other non-current assets	1146.3	1214.4	1265.9	1322.6	Book Value	501.16	125.80	147.12	179.62
Current Investments	0.0	34.1	134.1	834.1	Free Cash Flow	-87.4	19.5	14.0	5.3
Current assets									
Inventories	4,870.9	5,090.5	6,156.0	7,885.2	Valuation Ratios				
Trade receivables	4,448.6	5,676.1	6,906.3	8,174.5	P/E(x)	7.4	34.8	26.5	17.7
Cash and bank balance	287.7	104.6	261.1	824.7	P/B(x)	8.3	4.9	4.2	3.5
Total Loans & Advances	90.7	188.5	226.2	271.4	EV/EBIDTA(x)	20.8	18.1	14.8	10.7
Other current assets	414.3	494.3	594.7	774.3	EV/SALES (x)	4.2	3.9	3.2	2.4
Total Current assets	9,824.5	11,449.2	13,883.1	17,105.4					
Current liabilities					FCF Yield(%)	-2%	3%	2%	1%
Trade payables	2476.1	2631.0	3131.4	3948.3					
Other current liabilities	1470.7	2087.7	2356.8	2734.6	Return Ratios (%)				
Short term provisions	76.5	101.2	121.8	158.6	ROE	17%	14%	16%	20%
Long term provisions	67.7	91.7	110.4	143.7	ROCE	15%	15%	17%	21%
Total Current Liabilities	4091.0	4911.7	5720.4	6985.2					
Working Capital	5733.5	6537.6	8162.8	10120.2					
CAPITAL DEPLOYED	18,144.2	21,622.5	23,520.3	27,026.7					



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