Investor's delight: J.B. Chemicals & Pharmaceuticals Limited (JBCPL) **29th February 2020**

CMP: Rs. 538| Target price: Rs. 663| Upside: 23%|FV: Rs. 2| Market Cap: Rs. 4,159 crores| BSE code: 506943|NSE code: JBCHEPHARM| Bloomberg code: JBCP:IN| Reuters code: JBCH.NS

One year Price movement chart

Source: Moneycontrol

Financial summary

Particulars - Rs. crores	FY16	FY17	FY18	FY19	FY20E	FY21E	FY22E
Net Sales	1,210	1,344	1,409	1,643	1,807	2,014	2,256
YoY growth (%)	5.8	11	4.8	16.6	10	11.5	12
EBITDA	206	232	218	306	360	425	492
EBITDA (%)	17.0	17.26	15.47	18.62	19.9	21.1	21.8
PAT	162	184	141	195	260	302	361
PAT (%)	13.38	13.69	10.00	11.87	14.38	15	16
EPS (Rs.)	19.1	21.69	16.88	24.43	33.63	39	46.7
P/E (x)	29	26	33	23	17	14	12
Equity share capital	16.96	16.96	16.71	16.05	15.46	15.46	15.46
Reserves	1,167	1,347	1,425	1,464	1,580	1,827	2,133
Networth	1,184	1,364	1,442	1,480	1,595	1,842	2,148
Book value (BV) Rs.	140	161	173	184	204	238	278
P/BV (x)	4	3.5	3.2	3	2.5	2.1	1.8
RoE (%)	13.68	13.48	9.78	13.17	14.9	15.7	15.1
Receivables days	82	72	78	69	67	65	65
Inventory days	57	54	55	54	52	50	50
Payable days	76	64	34	23	25	25	25

Source: Company, Ajcon Research

Investment Rationale and Recommendation..

We are initiating coverage on J.B Chemicals and Pharmaceuticals Ltd. (JBCPL) as the Company's domestic formulation business is doing good and overall 9MFY20 performance has been robust. For nine months ended financial year 2020, the Company's consolidated net revenue was around Rs.1,331 crores, registering a growth of 9% on year-on-year basis. Absolute year-to-date operating EBITDA reported year-on-year growth of 19% at Rs.285 crores and EBITDA margin stood at 21.9%. Net profit for the company increased to Rs.222 crores, reporting a growth of 51% on year-on-year basis.

Research report written by - Akash Jain, MBA (Financial Markets), Vice – President Research

In addition, the Company's presence in US is small and all their US FDA approved plants are not facing any major regulatory actions. Company's US FDA approved solid oral dosage forms formulations manufacturing facility at Panoli, Gujarat has successfully passed periodical inspection by US FDA with one minor procedural observation. This observation does not impact continuity of Company's business and the Company would continue its manufacturing activities in cGMP compliant manner. The said inspection was carried-out from 3rd February 2020 to 7th February 2020. This is the 10th consecutive successful inspection for this facility.

The company was incorporated in 1976 under the chairmanship of legendary Mr. J.B Mody. Over the past four decades JBCPL has established brands not only in India but also internationally to 30+ countries, supplying affordable and quality products.

The company is well known for supplying quality products spread across chronic and acute therapeutic segments like cardiovascular, gastro, anti-infective, pain management.

The company manufactures a wide range of innovative specialty products across dosage forms like tablets, injectable, creams & ointments, lozenges, herbal liquids and capsules. The company has 8 manufacturing facilities across Gujarat and Daman, with USFDA approved Tablet plant and API plants. The R & D facilities are DSIR approved located in Maharashtra, Gujarat and Daman. The domestic business which comprises of Branded Generics and Contrast Media contribute approximately 45% of its consolidated revenue. The international business contributes to the balance 55% of revenue and comprises of branded generics, contract manufacturing, ANDAs and APIs. There are concerns over Ranitidine business after GSK's global decision to recall the drug. The Company's topline growth from Ranitidine business was flat in Q3FY20 segment but the management expects it to recover soon. The management has clarified, it is a safe drug and the impurity levels in the drug are within USFDA limits. South Africa business is expected to do well in the coming years. The recent successful Buyback by the Company also instills confidence as it enhances shareholders value. The Company has a strong Balance sheet and virtually debt free. There are no major capex plans apart from maintenance capex of around Rs. 50 crores p.a which will keep double digit ROE intact and scope for further improvement.

At **CMP of Rs. 538**, the stock is valued at a **P/E of 17x at estimated FY20 EPS of Rs. 33.63**. We recommend a "Buy" with a target price of **Rs. 663 (17x at estimated FY21 EPS of Rs. 39)** with investors of **9-12** months horizon, implying **an upside of 23.2%.**

Domestic business driving growth..

The domestic business which comprises of Branded Generics and Contrast Media (dyes that are injected during MRI, an angiography, CT scan - R& D based products which is used for investigative purposes in cath labs as in MRI centers) contribute approximately 45% of its consolidated revenue. The Company's international business contributes to the balance 55% of revenue and comprises of branded generics, contract manufacturing, ANDAs and APIs.

Domestic formulations business continued to grow at better than industry rate for fifth year in running. With sales of Rs. 622.54 crores in FY19, the domestic formulations business achieved growth of 14.5% against the industry growth of 11% (IQVIA, March 2019), while focus products registered growth of 22%. It is fifth year in running where the Company's domestic formulations business has grown at better than industry growth rate.

The Company's key therapeutic segments viz. Cardiovascular and Gastroenterology were the main growth contributor as they registered growth of 25% and 10% respectively.

The Company's key products: Cilacar (calcium channel blocker) with sales of Rs. 199 crores registered growth of 27%, while Rantac products group (anti-peptic ulcerant) with sales of Rs. 159 crores registered growth of 13%. The other key products group viz. Metrogyl with sales of Rs. 92 crores and Nicardia with sales of Rs. 52 crores also continued to grow well. The Company is ranked 34th in the domestic industry with Company's four brands viz., Rantac (anti-peptic ulcerant), Metrogyl (amoebicides), Cilacar (calcium channel blocker) and Nicardia (calcium channel blocker) featuring in top 200 brands in unit terms, while Rantac and Cilacar also feature in top 100 brands in value terms. Overall, the Company is heavily dependent on its top four brands which contribute 81% of its domestic revenue

In these existing four brands, the growth is largely penetration-driven as now each of the teams manage these brands individually as compared to one large team managing so many brands earlier. As a result, the focus in the therapy improves, the relationship with the doctors improves as well which is driving results for the Company. Creation of four therapy focused divisions in this business supported by increase in size of the field force and aggressive scientific promotion has helped achieve the growth. This divisionalisation of team has helped place the right focus on the products leading to increase in productivity. In addition, the divisionalisation has helped create capacity to efficiently handle more products in the future.

The Company recently hiked prices of its key brand "Metrogyl". According to the Management there are 4 SKUs and one of them has already started in the beginning of this month. It is expected that by mid of March new prices will be in the market.

In FY20 for domestic business, the Company launched new products across various segments which have good growth opportunity. In cardiovascular segment, the Company has introduced ARBs which is candesartan, introduced a beta blocker which is Atenolol and introduced Cadexomer under the brand name Cadomer. The new products that are being added would be categorised under the same division, so there won't be much addition to the salesforce of the company which would not add to the cost and improve MR productivity. In the short term, the Company now plans to consolidate the business with selective additions to field force as warranted for enhancing operations of any division, and leverage the sales by regular introduction of new products.

Overall for domestic business 12% growth is from price hike, volume contributes to ~9% and 1-2% is from new introduction. For the Domestic business, the Company's management expects to maintain similar growth rate and expects the business will grow faster than the market. As far as domestic business margins are concerned, the management expects it to remain flat as there maybe a couple of expansions that JCPL may do in the coming year.

Ranitidine business affected in Q3FY20 but would recover soon..
Ranitidine business was impacted after GSK Pharma's decision to discontinue "Ranitidine" products globally. Many drug regulators across the globe have banned the sale and manufacturing of anti-acidic drug ranitidine until its safety profile is verified and assured, the Drug Controller General of India (DCGI) has only alerted the state drug authorities to direct the manufacturers to ensure patient safety. The Health Sciences Authority of Singapore had found unacceptable levels of nitrosamine. In India, over 180 products based on ranitidine are sold by various leading drug makers with market size of ~ Rs. 750 crores. Ranitidine, an old molecule, is prescribed for intestinal and stomach ulcers, Gastroesophageal Reflux Disease (GERD), esophagitis, Zollinger-Ellison syndrome and others. Globally, the sale of this drug is over US$412 million. In India, Dr Reddy's Laboratories was the first to voluntarily suspend all distribution of its ranitidine as a precautionary measure. Globally, GlaxoSmithKline voluntarily withdrew the drug as a precaution. While many drug regulators across the globe have banned the sale and manufacturing of Ranitidine until its safety profile is verified and assured, the Drug Controller General of India (DCGI) has only alerted the state drug authorities to direct the manufacturers to ensure patient safety.

In India there are three large manufacturers - Cadila, GSK and JBCPL.

According to the Management, Ranitidine has been in the market for the last 35-years and the doctors have comfort in this product and believe that the product is relevant, important and needs to continue. Currently, the controversy that has been created for this impurity is the level that today USFDA is talking about.

According to USFDA, if a patient takes Ranitidine continuously for 70-years, one out of 1 lakh patients has the probability of generating cancer. The probability itself is low, MDM has a normal impurity that is present in foods, etc. The Company has ANDA approval for Ranitidine tablets in the US, but it has not launched it yet because of the DMA issue. USFDA is working with the API supplier and the API supplier has to reply to the queries.

The Company will be able to launch it in the US once the queries are satisfactorily answered by the API supplier and then USFDA communicates to the Company. In other markets, wherever there has been an issue, the Company has stopped supplies there but that is very small in the other export markets. There is a bit of revival in Domestic business towards the December but still there is a bit of challenge on the Ranitidine business.

Contract manufacturing business to do well..
To expand its revenue stream, the Company is trying to expand its contract manufacturing business and is working with few MNCs. In the past, JBCPL had few issues with one of the Russian companies which is expected to get resolved in the year going forward. Further, the company is constantly putting efforts to get new clients to add to the basket which will further deliver growth in this segment.

ANDA approvals
Till date, the company has got 16 approvals till date and there are 3 approvals which are pending with the FDA and the company plans to file 2 ANDAs per year, going forward.

Exports
JBCPL manufactures generic products for the regulated markets and branded formulations for the emerging markets. The company sells products under its own brand as branded generics and sells private labels under its customers' brand names. As large-scale suppliers of tablets, capsules, creams & ointments, injectables, liquid herbal syrups and lozenges, JBCPL is renowned world-wide for its commitment to quality and on-time delivery. Generics are exported to USA, UK, South Africa, Australia and Canada and branded generics are exported to parts of Africa, South-east Asia, Gulf, the Middle East, Central &

South America. The Company is amongst India's top 20 pharmaceutical formulation exporters with distributors across various countries. JBCPL has ANDAs approved in the US and sells those ANDAs through marketing partners.

The Company's total formulations exports in FY19 stood at Rs. 686.51 crores (growth of 27.6% over FY18). Exports to Global markets (other than Russia-CIS) at Rs. 484.88 crores registered growth of 21.80% in Rupee terms and 12.10% in US dollar terms over the previous year. The sales to US at Rs. 179.22 crores registered growth of 66.80% with Glipizide sales being the major contributor. Besides US, sales to South Africa, Africa and South-East Asia also fared well. US business and contract manufacturing business continue to do well. These are focussed business activities in formulations exports business and the Company has been investing accordingly

Total formulation exports stood at Rs. 686.51 crores in FY19.

US business: FY19 topline Rs. 179.22 crores
The market situation in the United States is not very encouraging as it is facing challenges of pricing. The company has not been very aggressive and has been very cautious. The company's plan is to limit the R&D spending going ahead. For the first nine months of FY20, US business was slightly impacted because one of its ANDAs where the API supplier had some FDA queries. However, it is resolved as on date. As a result, Q4FY20 for that product (big contributor to US business) will be good as sales will resume. Going forward the formulations exports will continue to grow. US business will normalize again in the next quarter.

Russia and CIS markets: FY19 topline Rs. 115 crores
The Company considers Russian market as highly potential and is currently investing in new products for this market to grow the products basket. During FY19, the Company received a new product registration for Pantoprazole 20 mg. tablets in Russia. The Company plans to continue to pursue vigorous marketing initiatives in this market to build strong product basket.

The Company continues to contract manufacture and supply products to Cilag International GmbH to whom we sold our Russia-CIS OTC business.

OOO Unique Pharmaceutical Laboratories, Company's Russian subsidiary, registered growth of 10.64% in sales at 626.46 million Rouble in FY19, while its profit after tax at 19.18 million Rouble was also higher. Presently, Russian markets have concerns because of the sanctions which are imposed on the country. The market is not growing at a fast pace, but the company has a limited share of products which are registered and few are in the process of getting registered. The Russian subsidiary for the first nine months registered a growth of about 21%. Going forward the company believes that things would change as they get their approvals. In the Russian market, the Company has 7-10 products which are currently registered in the market and the company has 4-5 products under approval which should come in this year. According to the Management, there is pressure in CIS markets too owing to their dependence on Russia. However, the Management is hopeful that things will change in the next six months to a year down the line.

South Africa: FY19 topline Rs. 156 crores
Historically, South Africa has done well for the Company over the last 12 years. The Company was first to enter South African market. The Company has grown at a CAGR of 15% year-on-year. For FY19, the South Africa business recorded a topline of Rs. 156 crores (331.97 mn Rand (US$ 22.03 mn – Rs. 156 crores at Rs 71 per US Dollar). Biotech Laboratories (Pty.) Ltd. ("Biotech"), Company's South African subsidiary, registered growth of 20.76% in sales at 331.97 million Rand and its profit after tax at 20.83 million Rand registered growth of 38.51% and the management expects this trend to continue. Private market as well as the public tenders continues to do well for the Company. Despite a sluggish South African economy and a volatile Rand/Dollar exchange rate, Biotech managed to increase sales by 20.76% compared to the previous year. This increase was driven by unit market share gains within the private market sector where growth of 36% year-on-year in value was achieved.

Biotech's relationship with the major retail pharmacy chains continues to grow and contributed to this success. Government purchasing was muted but sales to this customer still recorded growth of 15% year-on-year). The Company expects the South Africa business to do well in future.

Key challenges faced in domestic and international market..
In the domestic market, the Company faces challenges like stiff competition in the market place, Government approach to drug pricing, generic drugs and its stand on fixed dose combinations. For the international business, currency volatility and changing regulatory environment are the key challenges. With focus on scaling up of domestic formulations business on one hand, and growing Global business in US, Australia, South Africa and other key markets and lucrative contract manufacturing business, the Company is hopeful good growth going forward.

Key Manufacturing facilities

The company has 8 manufacturing facilities across Gujarat and Daman, with USFDA approved Tablet plant and API plants. The R & D facilities are DSIR approved located in Maharashtra, Gujarat and Daman.

State-of-the-art Formulations manufacturing facility at Panoli, Gujarat

State-of-the-art US FDA approved API facility at Panoli, Gujarat

State-of-the-art Tablets and Lozenges manufacturing facility at Kadaiya, Daman

Source: Company

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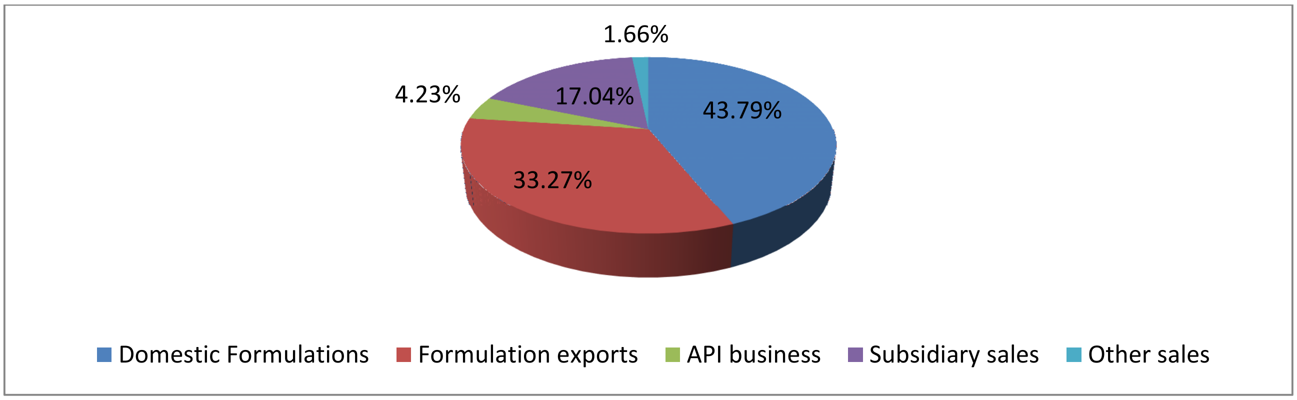
Q3FY20 result update

Consolidated sales performance (Rs. in crores)

Particulars	**Q3FY20**	**Q3FY19**	**% change**	**9MFY20**	**9MFY19**	**% change**
Domestic formulations	**183.97**	**161.15**	**14.16**	**595.00**	**512.73**	**16.04**
% of total sales	*43.79*	*43.21*		*45.64*	*42.79*	
Formulations exports	**139.76**	**133.07**	**5.02**	**449.39**	**442.76**	**1.50**
% of total sales	*33.27*	*35.67*		*34.47*	36.95	
API business	**17.78**	**19.49**	**(8.77)**	**56.56**	**58.13**	**(2.70)**
% of total sales	*4.23*	5.23		*4.34*	4.85	
Subsidiary sales	**71.57**	**54.92**	**30.32**	**184.50**	**169.98**	**8.54**
% of total sales	*17.04*	14.73		*14.15*	14.18	
Other sales	**6.96**	**4.23**	**64.53**	**18.21**	**14.62**	**24.56**
% of total sales	*1.66*	*1.13*		*1.40*	1.22	
Total	**420.04**	**372.86**	**12.65**	**1,303.66**	**1,198.22**	**8.80**

Source: Company, Ajcon Research



Q3FY20 Consolidated financial performance

Particulars	**Q3FY20**	**Q3FY19**	**YoY % change**	**9MFY20**	**9MFY19**	**% change**
Net sales	**420**	**373**	**12.7**	**1,304**	**1,198**	**8.8**
Operating income	9	10	(6.3)	27	26	5.5
Total Income	**429**	**383**	12.2	**1,331**	**1,224**	8.7
Cost of materials	150	126	19	484	432	11.9
Gross Profit	**278**	**257**	8.9	**847**	**792**	7.0
Employee expenses	82	72	13.9	237	213	11.2
Other expenses	109	105	3.2	325	332	(2.0)
Exchange. Fluctuation (Gain)/Loss	(2.24)	0.14	**-**	-		115.5
EBITDA	**90**	**80**	**14.9**	**286**	**240**	**18.9**
EBITDA (%)	**21.43**	**21.45**	**(2) bps**	**21.93**	**19.61**	**232 bps**
Finance cost	0.85	1.3	(34.2)	2.5	3.3	(24.2)
Depreciation	17	**15**	14.2	49	44	11.1
Profit before Tax before OI	**72**	**63**	**16.1**	**234**	**193**	**21.5**
Other income (OI)	16	16	**-**	47	26	84.2
Profit before tax	**88**	**79**	**13**	**282**	**219**	28.9
Prov. For tax (Net)	22	28	(21.4)	60	72	(16.8)
Profit after tax	**66**	**50**	**33**	**222**	**147**	51.1
Diluted EPS (Rs.)	**8.26**	**6.07**	**36**	**27.66**	**17.86**	**54.8**
Other comprehensive income	7	(6.31)		3	(7)	**-**
Total Comprehensive Income after tax	**73**	**44**	**68.2**	**225**	**140**	**60.7**

Source: Company, Ajcon Research

The consolidated net revenue in Q3FY20 witnessed a growth of 12.7 percent to Rs.420 crores on year-on-year basis led by domestic formulations business which grew by around 14% quarter-on-quarter on year basis and also the branded generics export which grew by about 17% on year-on-year basis.

EBITDA registered a growth of 15% touch Rs.89.6 crores. EBITDA margins stood around 21.3% as against 20.9% for the same period last year owing to cost optimization which was seen in the form of reduction of other expenses. The company reported net profit of Rs.66 crores which grew by 33% on year-on-year basis.

For nine months ended financial year 2020, the Company's consolidated net revenue was around Rs.1,331 crores, registering a growth of 9% on year-on-year basis. Absolute year-to-date operating EBITDA reported year-on-year growth of 19% at Rs.285 crores and EBITDA margin stood at 21.9%. Net profit for the company increased to Rs.222 crores, reporting a growth of 51% on year-on-year basis.

No major threat from Coronavirus outbreak as dependence on of Imports from China is fairly small and the domestic substitutes are available..

The Company's import kitty is small. Out of total material cost, about Rs.100-120 crores is worth an import material, rest all are domestically procured. But out of these Rs.100 crores worth of Company's import almost 70% to 75% comes from China.

There are two parts of this, firstly the API that the company directly procures from China and secondly, 2 key raw materials that the company procures for APIs. So the company is looking at the entire list of APIs in both the categories and this time the plan is to add inventory, if necessary and make sure that if the supply chain gets interrupted, JB Chemicals' business is not affected. As on date, the Company has enough inventory for 2 months. Further, the company is also looking for alternatives but switching suppliers in pharmaceutical industry as it is a long process which is not easy. There are domestic suppliers of APIs as well which Company can target in case of major supply chain disruption continues even after 2 months.

Buyout of trademarks from Unique Pharmaceuticals to be EPS accretive..

The company has trademarks licensing arrangement with Unique Pharmaceutical Laboratories Limited under which company has licensed several brands named under "Unique" logo and company has been annually paying restricted royalty of about Rs.10 crores for last several years. Unique Pharmaceutical Laboratories has agreed to sell and the board of directors of the company has approved to purchase the entire trademark portfolio of Unique Pharmaceutical Laboratories at one-time consideration of Rs.8 crores. This transaction will be consummated before the end of this financial year. Consequently, the aforesaid licensing arrangement will stand submitted as such and there would be no royalty payment beginning next financial year and hence this would be an EPS-accretive to J.B. Chemicals and Pharmaceuticals Limited from next financial year.

Focusing on MR productivity..

The Company has completed restructuring exercise and has done about 100-odd people during the last year. As a result, business units would have enough opportunity to grow. The activities within the team will be continuing to enhance productivity which is whatever revenue growth we get, it will be going directly to the productivity.

Buy - back of equity shares completed successfully increasing shareholder's confidence..

Recently, the Company completed buy-back of 29,54,545 shares at Rs. 440 per share on January, 08 2020. The paid-up equity share capital now stand at 7,72,82,097 equity shares of Rs. 2 each.

In FY19, the Company completed buy-back of up to 3,333,333 equity shares of the Company at Rs. 390 per share, which received good response from the shareholders which resulted in outgo close to Rs.130 crores excluding transaction costs.

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Date: 2020.02.29 12:03:26 +05'30'