YES SECURITIES
INSTITUTIONAL EQUITIES

March 06, 2024

COMPANY REPORT | Sector: Pharmaceuticals

JB Chemicals & Pharma

Lozenges plant visit KTAs

Reco	:	ADD
CMP	:	Rs 1,571
Target Price	:	Rs 1,720
Potential Return	:	+10%

We hosted investors for a visit to JB Chemicals' Daman lozenges facility to better understand the outlook for lozenges business and factors that can drive growth. Key takeaways include 1) Geographical expansion with same customer, tech transfer for customer owned product and owned product push are three main levers of growth 2) Companies want to do quick marketing and not earlier practice of filing of own dossiers which is leading to quicker but durable demand 3) Overall 50% by volume is JB Chem IP (owned developed products) and rest is customer who has brought in the tech transfer or products 4) Growth of top 5 customers has doubled in volumes with 70% share of top 5 customers 5) Switching takes at least 2-3 years which explains lack of client churn since inception 6) Many of the products currently sold in India would not be feasible in JB Chemicals facility given the multiple regulatory approvals garnered by the facility. 7) Return on capital invested would never be commensurate with scale achievable in the near term and it is always a long term business. Key learning was while lozenges business does not have manufacturing complexity, primary barrier is the relationship built with customers over 2 decades and would be difficult to disrupt. Overall, JB Chem should report margin impact in Q4 due to payment for acquired ophthalmology portfolio even as rebound in acute season is eyed from Q1 FY25. Since there is no change to growth expectation but recent correction has bought stock in to a semblance of comfort zone, raise our rating to ADD from Reduce with largely unchanged TP Rs1,720, based on 30x FY26 EPS.

3 ways to grow – geographical, tech transfer and owned development

Lozenges business presents several different ways to drive growth. Addition of geographical region is the quickest way to expand lozenges business and JB has been adding territories for some of the largest global consumer oriented companies. Tech transfer involves sharing of product and composition know how from the customer to be further built on by JB. Pushing owned developed IP and products is the third and probably the toughest way to grow as customer conversion takes a long time. About ~50% share by volume is linked to products where JB has the IP leading to better pricing. Pertinent to note is even if the product belongs to JB, it does not share identical composition with other customers to avoid conflict with existing partner.

Relatively simple manufacturing: long standing relationships act as barrier to entry

Our lozenges visit shows manufacturing complexity is unlikely to be a key barrier to building CMO business; moreover, reckon JB may not have cumulatively invested more than Rs1.2-1.3bn (excluding the recently purchased land adjacent to current unit), which leaves strength of relationships build over 2 decades as the key differentiator. Indeed, in building a lozenges business, even in the medium term say 3-5 years, the volume offtake does not justify putting up the capacity. Only over a long period of time, does the value of front loading capacity appears to be value additive. As a corollary, JB has never lost a client since inception, an indication of the customer stickiness.

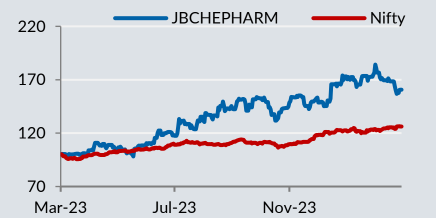
Recent correction brings valuation within comfort zone; raise rating to ADD

Expect CMO business to be subdued in FY24 followed by a rebound next fiscal. We incorporate Rs1.25bn payment to Novartis for marketing and distribution in Q4 as JB Chem begins to market the acquired ophthalmic portfolio. JB has largely put in growth and margin performance along expected line which in turn implies the estimated FY25 EPS (~Rs47 in Q1 FY24 to Rs46.7 in Q3 FY24 for FY25) has not undergone any material change. Continue to value JB Chem at ~30x but recent correction brings the stock into some semblance of comfort zone, and we retain largely unchanged TP Rs1,720 based on 30x FY26 EPS.

Stock data (as on March 05, 2024)

Nifty	22,356
52 Week h/l (Rs)	1940 / 875
Market cap (Rs/USD mn)	243192 / 2935
Outstanding Shares (mn)	155
6m Avg t/o (Rs mn):	237
Div yield (%):	0.5
Bloomberg code:	JBCP IN
NSE code:	JBCHEPHARM

Stock performance



	1M	3M	1Y
Absolute return	-9.1%	5.2%	60.6%

Shareholding pattern (As of Dec'23 end)

Promoter	53.8%
FII+DII	28.9%
Others	17.3%

Δ in stance

(1-Yr)	New	Old
Rating	ADD	REDUCE
Target Price	1,720	1,700

Δ in earnings estimates

	FY24e	FY25e	FY26e
EPS (New)	32.2	46.7	57.3
EPS (Old)	32.2	46.7	57.3
% change	-	-	-

Financial Summary

(Rs mn)	FY24E	FY25E	FY26E
Net Revenue	35,185	41,390	46,951
YoY Growth	11.7	17.6	13.4
EBIDTA	8,680	11,699	13,646
YoY Growth	13.5	34.8	16.6
PAT	4,971	7,216	8,864
YoY Growth	21.3	45.1	22.9
ROE	20.8	25.6	24.8
EPS	32.2	46.7	57.3
P/E	48.9	33.7	27.4
P/B	9.0	7.4	6.0
EV/EBITDA	27.9	20.3	17.0

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JB Chemicals & Pharma

- Daman facility visit KTAs and interaction with plant head
- Daman facility houses lozenges and some bit of capacity in tablets for domestic markets. Except for US FDA, facility has most other important certifications including EU GMP. Below are the key takeaways from the visit and our interaction with plant head Mr Parmeshwar Bang
- Facility caters to large consumer oriented customers
- About 40% of the lozenges business is development led where JB has done the development part in the past and owns the IP. Obviously, margin on such products would be higher than rest of lozenges portfolio
- There is no major difference in growth rates between owned developed-led manufacturing and pure CMO
- Manufacturing capacity of ~2.4bn lozenges and doing 1.1bn per annum
- Cilacar T and Rantac are also manufactured at the facility
- Total of 2 manufacturing and 9 packing lines. Putting a single line today might require Rs400mn. Even so, more than capital, it is ability to evolve and partner with customers is what is the key in lozenges
- Blisters form 70-80% of the volumes and looking to expand capacity in the same
- Do not market lozenges in domestic market; Zeecuf brand would be closest competition to Strepsils
- Given the strength of relationship, cross marketing is happening as one company strong in say China is looking to partner someone strong in other region and vice versa.
- Overall, 50% is JB Chem IP and rest is customer who has brought in the tech transfer or products vol wise.
- Growth of top 5 customers by volume has doubled and accounts for 70% share
- Contract duration for each customer is different and even CB-30 is applicable like in pharma. Switching takes at least 2-3 years.
- Initial manufacturing losses are the same irrespective of the batch size so larger the batch size better it is for the company.
- Even if the molecule is off patent even so do not give the same composition to other customers. Large players in India like a Ahmedabad based player who is working at least 2 decades prior to JB Chem. But believe those facilities are meant only for India approved products.
- Many of the products currently sold in India would not be feasible in JB Chemicals facility given the multiple regulatory approvals garnered by the facility.
- Return on capital invested would never be commensurate with scale achievable in the near term and it is always long term business.
- No churn has been observed in the business. At the start vols are always lower which needs time to ramp up. Plus, pricing is also lower than pharma product so volumes need to reach scale more than those attained by pharma molecules.
- Customers see the capability and capacity to support over a long period of time.
- Quality is another area which requires investment in the form of GC and HPLCs.

FINANCIALS

Exhibit 1: Balance sheet

Y/e 31 Mar (Rs m)	FY22	FY23	FY24E	FY25E	FY26E
Equity capital	155	155	155	155	155
Reserves	21,187	24,649	26,876	32,719	40,212
Net worth	**21,341**	**24,804**	**27,030**	**32,874**	**40,366**
Debt	375	4,163	4,163	4,163	4,163
MI	45	0	0	0	0
Def.tax lia	476	1,028	1,028	1,028	1,028
Total liabilities	**22,236**	**29,994**	**32,221**	**38,065**	**45,557**
Goodwill	575	575	575	575	575
Fixed assets	12,382	18,987	18,448	17,922	17,348
Investments	304	632	632	632	632
Net working capital	**8,911**	**9,736**	**12,502**	**18,871**	**26,938**
Inventories	4,100	4,305	4,810	5,658	6,418
Sundry debtors	5,557	5,758	6,433	7,568	8,584
Cash	585	2,710	4,503	9,155	15,683
Other current assets	2,507	2,508	2,815	3,311	3,756
Sundry creditors	(2,245)	(2,386)	(2,666)	(3,136)	(3,558)
Other current liabilities	(1,592)	(3,158)	(3,393)	(3,684)	(3,946)
Def tax assets	64	65	65	65	65
Total assets	**22,236**	**29,994**	**32,221**	**38,065**	**45,557**

Exhibit 2: Income statement

Y/e 31 Mar (Rs m)	FY22	FY23	FY24E	FY25E	FY26E
Revenue	24,242	31,493	35,185	41,390	46,951
Operating profit	**6,211**	**7,648**	**8,680**	**11,699**	**13,646**
Depreciation	(727)	(1,144)	(1,289)	(1,276)	(1,324)
Interest expense	(51)	(361)	(472)	(472)	(472)
Other income	392	99	270	270	270
Profit before tax	**5,825**	**6,242**	**7,188**	**10,221**	**12,119**
Taxes	(1,189)	(1,452)	(1,797)	(2,555)	(3,030)
Adj Profit	**4,637**	**4,790**	**5,391**	**7,666**	**9,089**
Exceptional	(777)	(690)	(420)	(450)	(225)
Net profit	**3,860**	**4,100**	**4,971**	**7,216**	**8,864**

Exhibit 3: Cash flow statement

Y/e 31 Mar (Rs m)	FY22	FY23	FY24E	FY25E	FY26E
Profit before tax	5,825	6,242	7,188	10,221	12,119
Depreciation	727	1,144	1,289	1,276	1,324
Def.taxes (net)	(87)	552	-	-	-
Tax paid	(1,189)	(1,452)	(1,797)	(2,555)	(3,030)
Working capital Δ	(3,211)	1,300	(973)	(1,717)	(1,539)
Other operating items	(777)	(690)	(420)	(450)	(225)
Operating cashflow	1,288	7,096	5,288	6,774	8,650
Capital expenditure	(7,142)	(7,749)	(750)	(750)	(750)
Free cash flow	**(5,854)**	**(653)**	**4,538**	**6,024**	**7,900**
Equity raised	659	638	(0)	(0)	0
MI	8	(45)	-	-	-
Investments	(111)	(327)	-	-	-
Debt financing/disposal	149	3,788	-	-	-
Dividends	(1,275)	(1,275)	(2,744)	(1,372)	(1,372)
Net Δ in cash	**(6,425)**	**2,125**	**1,794**	**4,652**	**6,528**

Exhibit 4: Du Pont Analysis

Y/e 31 Mar (Rs m)	FY22	FY23	FY24E	FY25E	FY26E
Tax burden (x)	0.80	0.77	0.75	0.75	0.75
Interest burden (x)	0.99	0.95	0.94	0.96	0.96
EBIT margin (x)	0.24	0.21	0.22	0.26	0.27
Asset turnover (x)	1.03	1.04	0.97	1.01	0.97
Financial leverage (x)	1.20	1.31	1.40	1.37	1.32
RoE (%)	**23.5**	**20.8**	**20.8**	**25.6**	**24.8**

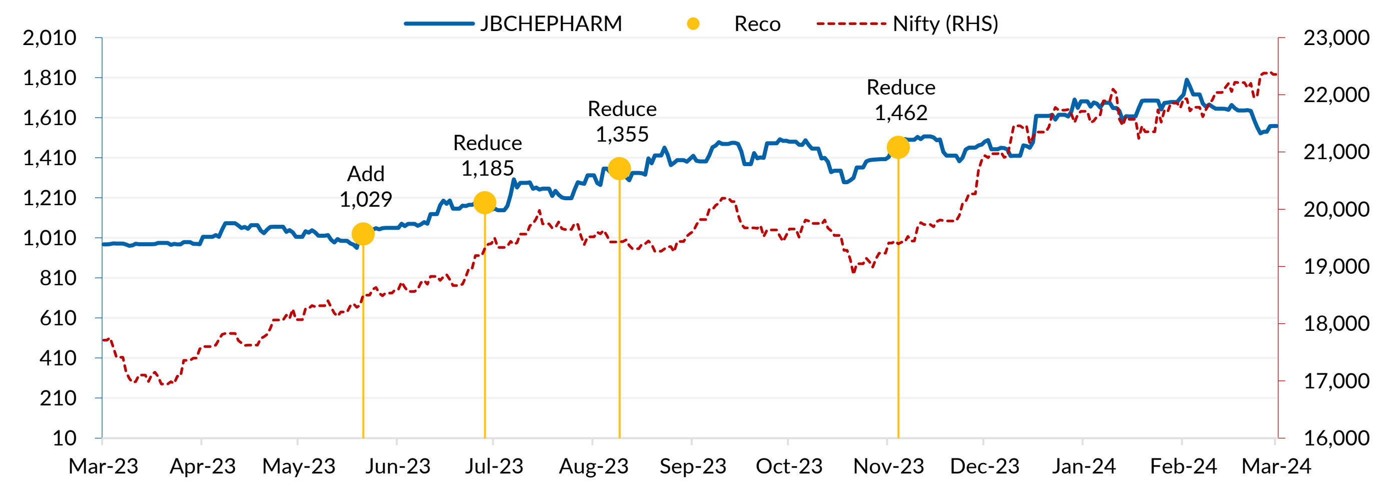
Exhibit 5: Ratio analysis

Y/e 31 Mar	FY22	FY23	FY24E	FY25E	FY26E
Growth matrix (%)					
Revenue growth	18.7	29.9	11.7	17.6	13.4
Op profit growth	10.8	23.1	13.5	34.8	16.6
EBIT growth	(2.7)	12.4	16.0	39.6	17.8
Net profit growth	(13.9)	6.2	21.2	45.1	22.9
Profitability ratios (%)					
OPM	25.6	24.3	24.7	28.3	29.1
EBIT margin	24.2	21.0	21.8	25.8	26.8
Net profit margin	19.1	15.2	15.3	18.5	19.4
RoCE	28.6	25.3	24.6	30.4	30.1
RoNW	23.5	20.8	20.8	25.6	24.8
RoA	19.7	15.9	14.9	18.7	18.8
Per share ratios					

JB Chemicals & Pharma

Y/e 31 Mar	FY22	FY23	FY24E	FY25E	FY26E
EPS	50.0	53.0	64.3	93.3	114.7
Dividend per share	16.5	16.5	35.5	17.8	17.8
Cash EPS	69.4	76.7	86.4	115.7	134.7
Book value per share	276.3	320.5	349.7	425.3	522.2
Valuation ratios (x)					
P/E	62.9	59.3	48.9	33.7	27.4
P/BV	22.8	19.6	9.0	7.4	6.0
M Cap/Sales	10.0	7.7	6.9	5.9	5.2
EV/EBIDTA	39.1	31.9	27.9	20.3	17.0
Payout (%)					
Tax payout	20.4	23.3	25.0	25.0	25.0
Dividend payout	33.0	31.1	55.2	19.0	15.5
Liquidity ratios					
Debtor days	84	67	67	67	67
Inventory days	62	50	50	50	50
Creditor days	34	28	28	28	28
Leverage ratios					
Interest coverage	114.8	18.3	16.2	22.6	26.7
Net debt / equity	(0.0)	0.1	(0.0)	(0.2)	(0.3)
Net debt / op. profit	(0.0)	0.2	(0.0)	(0.4)	(0.8)

Recommendation Tracker



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ADD: Upside between 10% to 20% over 12 months

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REDUCE: Downside between 0% to -10% over 12 months

SELL: Downside greater than -10% over 12 months

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