

# Strategy Memo

February 2024

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## A Strong Beginning to the Year Marked with Outperformance

The markets sustained their robust performance in Jan'24, building upon the momentum from the successful year of 2023. The Nifty 50 remained relatively flat for the month, experiencing a marginal decline of 0.03%. In contrast, our benchmark index, the BSE500 (TR) index, saw a notable gain of 1.92% over the same period.

It gives me immense pleasure to report that both our Pure Growth and Pure Contra strategies have started 2024 on a positive note and have outperformed their benchmark index – BSE500 TR in Jan'24. In Jan'24, both our Pure Growth and Pure Contra strategies outperformed their benchmark by 62bps and 299bps respectively (net of expenses). Over the past year, both strategies have consistently outperformed their respective benchmarks by 8.04% and 14.76%, respectively (net of expenses), a performance that we are extremely proud of.

In Jan'24, we observed that Energy, Utilities, Communications, Healthcare, Real Estate, Consumer Discretionary and IT outperformed the index while Financials, Consumer Staples and Materials underperformed the index and gave absolute negative returns for the month. Our Pure Growth strategy benefited from our overweight position in Consumer Discretionary, Communications, and Healthcare as well as our underweight position in Materials and Consumer Staples which contributed to positive alpha for the month. Stocks in this strategy that showcased notable outperformance included One97 Communications, Sun Pharma, Bharti Airtel, HPCL, Religare Enterprises, Indian Hotels, and Ajanta Pharma. On the flip side, Praj Industries, RBL Bank, Bandhan Bank, KDDL, Ultratech Cement, Kesoram Ind, Maruti Suzuki, and Linde India were amongst the main laggards.

In our Pure Contra strategy, our overweight calls on Consumer Discretionary, Utilities, Healthcare, and Communications and underweight calls on Financials and Consumer Staples helped us generate Alpha. Stocks that significantly contributed to achieving alpha included Thomas Cook, REC, Voltamp Transformers, Glaxo Pharma, Indian Hotels, HPCL, Tata Motors DVR, Indus Towers, Power Grid and Lupin, amongst others. On the other hand, Suven Pharma, RBL Bank, M&M, Maruti Suzuki, ITC and KDDL weighed on the overall performance of our portfolio.

In this strategy note, we will delve into one of the stocks that have demonstrated notable outperformance in recent times and remain a favoured component of our 'Pure Contra' strategy – **'Lupin Ltd'**.



*Nishit, through his diverse experience in both Buy side and Sell side firms brings in a fresh perspective on markets at Axis Securities. As Fund Manager, he is responsible for generating superior risk adjusted returns for customers as per their mandate.*

*Nishit has more than 18 years of experience in the financial services industry and has worked with various companies like ING Investment Management, Kotak Mahindra Bank, Elara Capital, Reliance Securities, AnandRathi, MotilalOswal Financial Services etc.*

## Genesis

Lupin was established in 1968 by Mr. Desh Bandhu Gupta (DBG), a chemistry professor at BITS-Pilani, Rajasthan. Starting with humble beginnings, DBG borrowed Rs 5000 from his wife and launched the company with just two employees. Subsequently, with the support of bank funding, Lupin embarked on its manufacturing journey, initially producing folic acid and iron tablets for the Government of India's Mother and Child Health Program. Over time, the company expanded its manufacturing capabilities to include anti-TB drugs, which at one juncture accounted for one-third of Lupin's revenues, establishing the company as one of the largest anti-TB drug manufacturers globally. Lupin has now evolved into an Indian multinational pharmaceutical company headquartered in Mumbai, boasting a presence across 11 countries and 6 continents. The company's manufacturing prowess extends across 15 plants located in India, Mexico, the US, the Netherlands, and Brazil. Lupin's strategic focus areas encompass paediatrics, cardiovascular, anti-infectives, diabetology, asthma, and anti-TB medications.

## New Product-Led Growth in The US

Lupin's management has guided for high single-digit growth in the US business in FY25 followed by a double-digit growth in FY26, and it will be driven by significant launches planned by the company. In fact, should the company successfully launch certain oral solids based on patent litigation outcomes, the growth potential for FY25 alone could reach double digits. The company's commitment to research and development is evident, with expenditure exceeding 7% of its revenues. This investment is reflected in the robust product launch pipeline anticipated for the next few years.

The company plans to launch 10+ products in the US in FY25, including a few interesting injectables such as Glucagon and Fosphenytoin along with good launches in the ophthalmic segment comprising products like Prolensa and Loteprednol. In the event of a favourable ruling on specific patent litigation, the company has the potential to launch certain oral solids such as Mirabegron and Slynd. In FY26, the company is

anticipated to introduce significant products, including Tolvaptan and Liraglutide, among others. The company's key product pipeline with significant market potential is given below:

## Key Pipeline for US Generic Products

Niche Generic Products	Market Size (\$Mn)	Lupin's Status	Potential Launch Timelines
Xyrem	~900 Mn	AG	CY24
Myrbetriq	~2400 Mn	Joint FTF with 180 days exclusivity	H1FY25
Sprycel	~1200 Mn	Para 4	H2FY25
Jynarque	~300 Mn	Joint FTF	CY25
Entresto	~1400 Mn	Joint FTF	CY25
Trijardy XR	~400 Mn	Para 4	FY26
Revlimid	~8000 Mn	Para 3	CY26

Source: Industry

Over the next few quarters, the management anticipates that the quarterly run-rate of US revenue will persist above \$200 Mn, with continued growth. Additionally, they foresee price erosion of generic oral solids to remain in the low single digits, attributed to shortages of drugs in key segments.

## India Business Expected to Outperform

Lupin's India business recorded strong double-digit growth in Q3FY24 with a 1.6x IPM growth rate. In most of its therapeutic areas like Respiratory, GI and Gynaecology, the company has outperformed IPM during the quarter. Lupin launched ~21 products in the year so far and as per IQVIA, it is ranked number one in new product launches in India. The company has a strong chronic focus, with more than 60% of sales contribution from chronic therapies. The management holds the belief that the company is strongly positioned to consistently deliver above-market growth in the future. This growth will be primarily driven by increased productivity stemming from sales force expansion, the introduction of new divisions, and improved penetration and reach in existing markets. For FY25, the management has guided outperformance of 20-30% as compared to the IPM growth. To this end, the company is doubling down on its India bet with a strong new product pipeline, especially in the Respiratory segment.

### Q3FY24 Results Surprised Positively

Lupin reported strong operating performance in Q3FY24 with a significant beat on consensus estimates across revenue, EBITDA, and PAT. The company's sales increased by 20.2% YoY to Rs 5,197 Cr, for the quarter and the growth was majorly led by its US business of \$212 Mn (~20% YoY growth in USD terms). The US sales continue to see encouraging traction in sales of gSuperb, gAlbuterol, gLisinopril, and new launches Darunivar (exclusivity in 800 mg) and gSpiriva (32% Market Share in the last 5 months) while the base business experienced low single-digit price erosion.

The India business (+13.4% YoY) outperformed IPM growth in key therapies such as CVS and anti-diabetic. The other segment reported growth as follows: EMEA (+36% YoY), and RoW business (+71.4% YoY). The company's gross margins were up 60bps QoQ and 630bps YoY to 66.8% due to a better product mix and strong growth in the US and Indian markets. Steady Staff cost and R&D cost offset by higher SG&A led to an EBITDA of Rs 1,038 Cr (+13.1% QoQ and +94.9% YoY) and a margin of 20%. Reported PAT increased to Rs 613 Cr (+25.1% QoQ and +299.4% YoY).

### Outlook, Financials and Valuations

We continue to remain positive on Lupin's prospects, underpinned by the following attributes: 1) Double-digit India growth driven by MR count and productivity, 2) Strong product pipeline for the US business, 3) Enhancement of the balance sheet through working capital optimization and debt reduction, and 4) Potential improvement in margins with improved efficiencies, falling raw material cost, and low single-digit price erosion in the US market for the base business.

Lupin trades at a reasonable valuation of 28.7x and 24.2x FY25 and FY26 estimates earnings respectively. We believe these to be reasonable multiples, especially if we factor in expected earnings growth of ~132% CAGR over FY23-26.

Particulars (Rs. Mn)	FY23	FY24E	FY25E	FY26E
Revenue	1,62,700	1,97,591	2,18,970	2,42,638
EBITDA	17,206	37,800	45,900	52,000
EBITDA Margins (%)	10.6	19.1	21.0	21.4
PAT	4301	21120	25200	29900
EPS (Rs/share)	9.5	46.4	55.4	65.7
PER (x)	168.2	34.3	28.7	24.2
BVPS (Rs/share)	274	312	356	409
P/BV (x)	5.8	5.1	4.5	3.9
RoE (%)	2.9	14.6	16.5	17.3
RoCE (%)	5.2	15.7	18.1	19.4

Source: Industry

### Risk to our thesis

- 1) Delays in product approvals
- 2) Regulatory risk with respect to USFDA audits for the plants
- 3) Pressure on margins in case of an increase in the cost of logistics and raw materials
- 4) Greater price erosion in the US base business, impacting future margins

### Happy Investing!

Nishit Master

## Summary of Portfolio Changes Made in Jan'24

In Jan'24, we made the following changes to both our portfolios to factor in the changing market dynamics.

### Growth Strategy changes

Scrip Name	Action	Weight	Remark
EClerx Services Ltd	BOUGHT	2.0%	Strong play on data analytics and process improvement solutions available at reasonable valuations
RBL BankLimited	SOLD	2.1%	Lowering allocation due to margin pressure and slight uptick in asset quality issues
ICICI BankLimited	SOLD	1.2%	Lowering allocation due to margin pressure

### Contra Strategy changes

Scrip Name	Action	Weight	Remark
Hindustan Petroleum Corporation Limited	BOUGHT	2.0%	Expect EBITDA to double on normalized numbers in three years on capacity expansion
Indus Tower Ltd	BOUGHT	1.0%	Indirect play on Idea, Vodafone's continuity of business
RBL Bank	SOLD	0.9%	Lowering allocation due to margin pressures and slight uptick in asset quality pressure

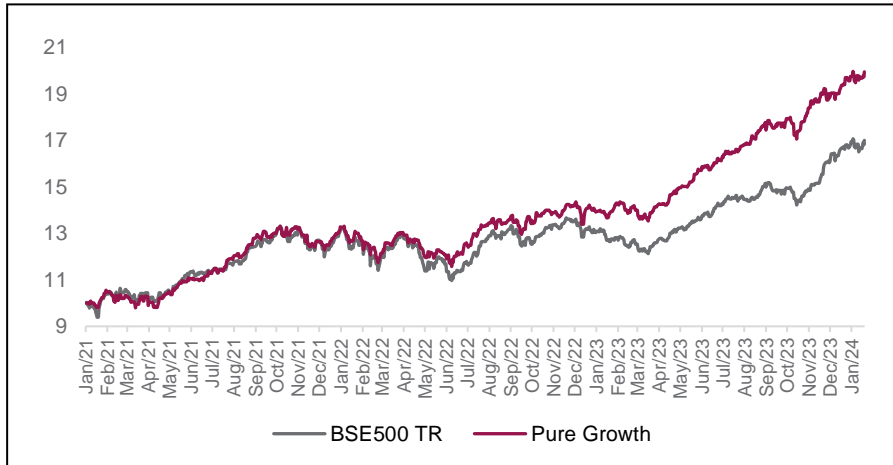
## MANAGED ACCOUNTS

## Axis Pure Growth

31<sup>st</sup> Jan 2024

**Investment Objective:** Axis Pure Growth strategy focuses on parameters comprising sustainable earnings growth, quality, and low volatility. The core investment styles are growth and quality investing while low volatility and alpha investing are other key styles employed depending on the macroeconomic regime.

## Cumulative Performance: Returns



## Annual Performance (%)

Year	Growth	BSE500 TR
2023 (YTD)	35.8%	26.8%
2022	8.7%	4.8%
2021 *	25.5%	25.8%

\*effective 13 Jan 2021

## Portfolio Performance

Particulars	1 month	3 months	6 months	1 year	2 years*	3 years*	Since inception**
<b>Growth</b>	2.54%	13.84%	18.49%	41.46%	22.86%	24.50%	23.23%
<b>BSE500 TR</b>	1.92%	17.88%	16.20%	33.42%	16.47%	21.89%	18.95%

(\*CAGR Returns) (\* Net of all charges) (\*\*Since 13th Jan. 2021)

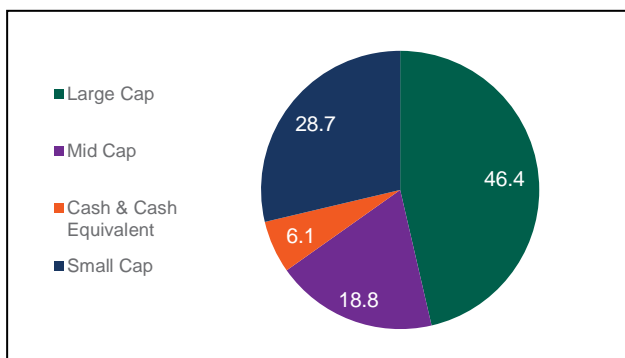
## Risk Assessment

	Growth	BSE500 TR
Sharpe Ratio	1.24	0.83
Volatility	13.0%	14.4%
Portfolio Beta	0.77	1
Max Drawdown	-13.2%	-17.6%
Information Ratio	0.56	
Average Turnover Ratio	1.48	

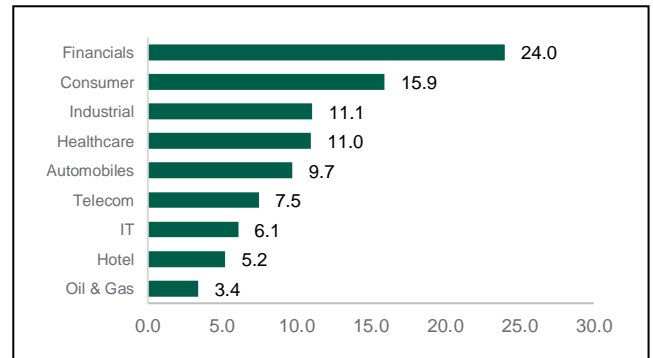
## Key Portfolio Ratios

	Growth	BSE500 TR
PE	34.12	18.67
PB	4.44	3.42
ROE	13.01%	13.13%
Dividend Yield	0.65%	1.11%

## Market Capitalization



## Sector Allocation



## MANAGED ACCOUNTS

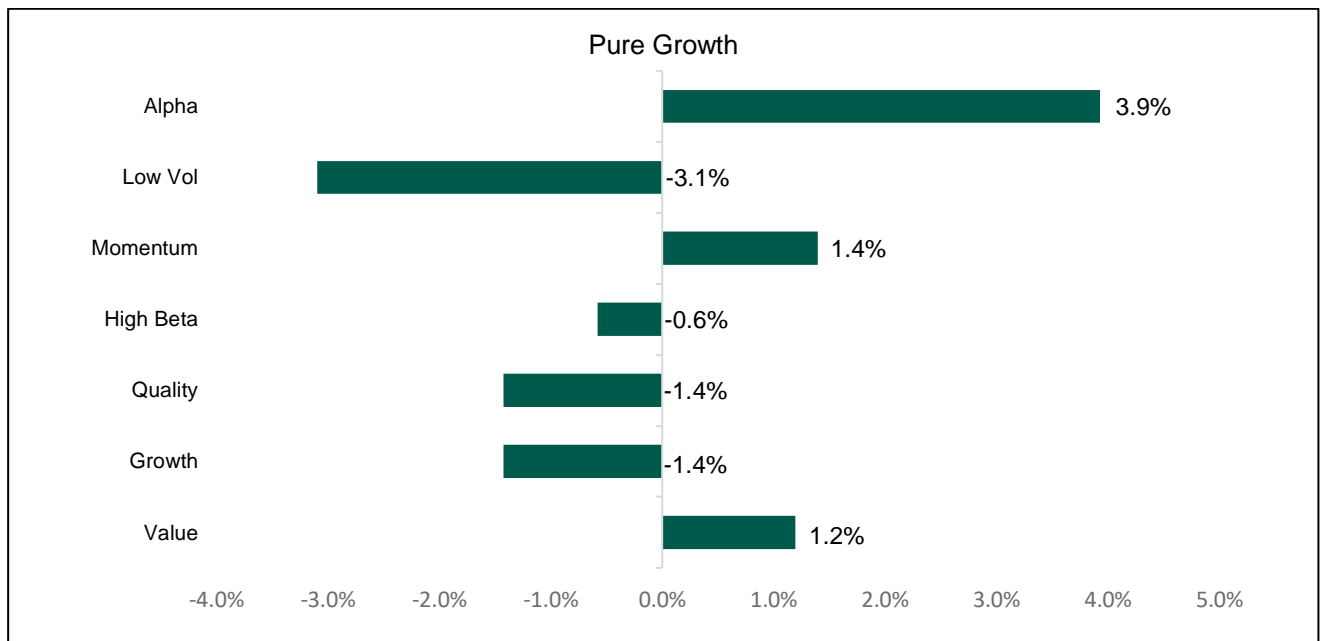
## Top 10 Holdings

Scrip Name	Market Cap (Cr)	Weight
Bharti Airtel Ltd	6,75,344	7.5%
Sun Pharmaceutical Indus	3,52,382	7.0%
Varun Beverages Ltd	1,73,946	6.3%
ICICI Bank Ltd	7,24,016	6.1%
Indian Hotels Co Ltd	72,118	5.2%
Gillette India Ltd	22,327	5.1%
Maruti Suzuki India Ltd	3,39,954	5.0%
Jio Financial Services Ltd	1,75,986	4.8%
CIE Automotive India Ltd	18,832	4.7%
KDDL Ltd	3,436	4.5%

## Portfolio Characteristics

	Growth
Number of constituents	22
Mcap Largest (Cr)	10,98,811
Mcap Smallest (Cr)	3,436
Mcap Average (Cr)	1,91,671
Mcap Median (Cr)	41,837

## Factor Box



The Factor Box provides relative factor exposure vis-à-vis a given benchmark. For instance, if the Growth factor exposure in a portfolio is 23% and the Growth factor exposure of the Benchmark is 20%, it indicates that your portfolio is "Overweight" on Growth with respect to the benchmark. A positive Value in the above Factor represents that the given portfolio is Overweight in the factor with respect to the benchmark. Similarly, a negative value would represent that the given portfolio is underweight in the factor with respect to the benchmark.

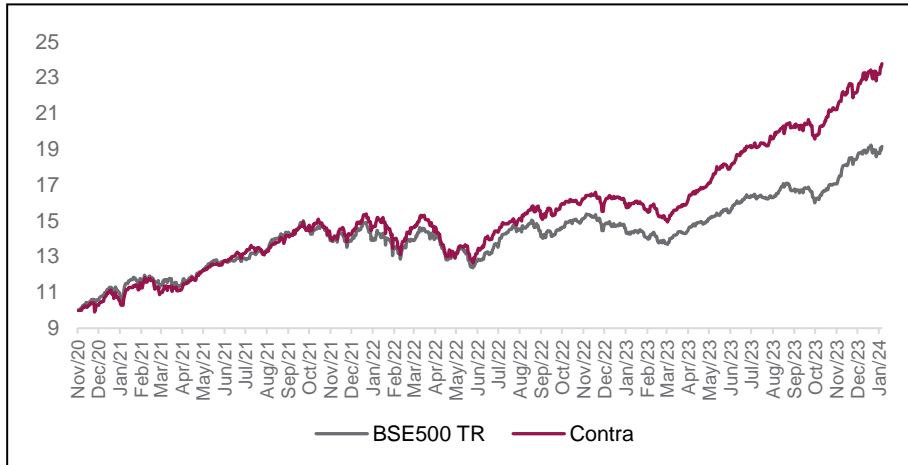
## MANAGED ACCOUNTS

## Axis Pure Contra

31<sup>st</sup> Jan2024

**Investment Objective:** Axis Pure Contra investment strategy focuses on three primary investment styles – Value, Momentum-Alpha, and Special situations investing. Value, Alpha-Momentum form the core factors while Special Situation investing is employed as a satellite factor.

## Cumulative Performance: Returns



## Annual Performance (%)

Year	Contra	BSE500 TR
2023 (YTD)	39.5%	26.8%
2022	9.7%	4.8%
2021*	36.5%	31.0%

\*effective 01 Jan 2021

## Portfolio Performance

Particulars	1 month	3 months	6 months	1 year	2 years*	3 years*	Since inception**
<b>Contra</b>	4.91%	19.95%	23.15%	48.18%	24.93%	30.58%	29.63%
<b>BSE500 TR</b>	1.92%	17.88%	16.20%	33.42%	16.47%	21.89%	22.81%

(\*CAGR Returns) (\* Net of all charges) (\*\*Since 27th Nov, 2020)

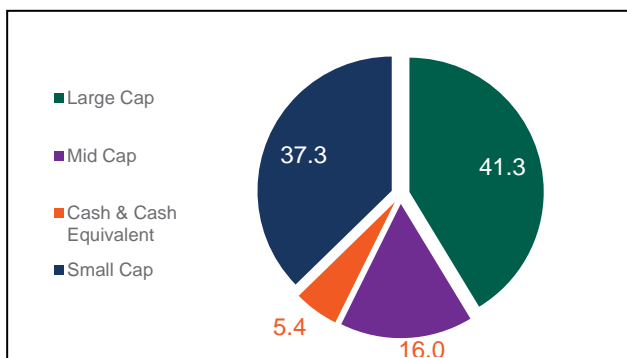
## Risk Assessment

	Contra	BSE500 TR
Sharpe Ratio	1.46	1.08
Volatility	15.4%	14.3%
Portfolio Beta	0.96	1
Max Drawdown	-17.9%	-17.6%
Information Ratio	1.02	
Average Turnover Ratio	1.90	

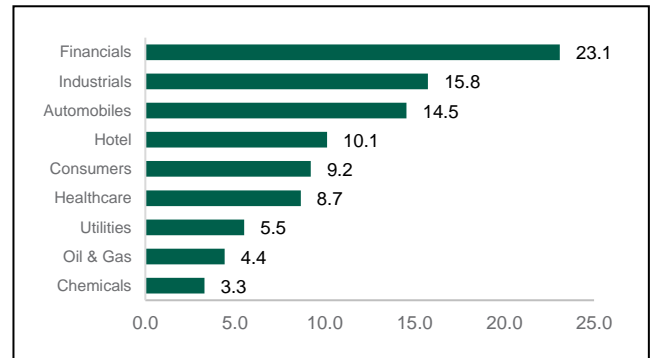
## Key Portfolio Ratios

	Contra	BSE500 TR
PE	18.75	18.67
PB	2.91	3.42
ROE	15.50%	13.13%
Dividend Yield	1.71%	1.11%

## Market Capitalization



## Sector Allocation





## MANAGED ACCOUNTS

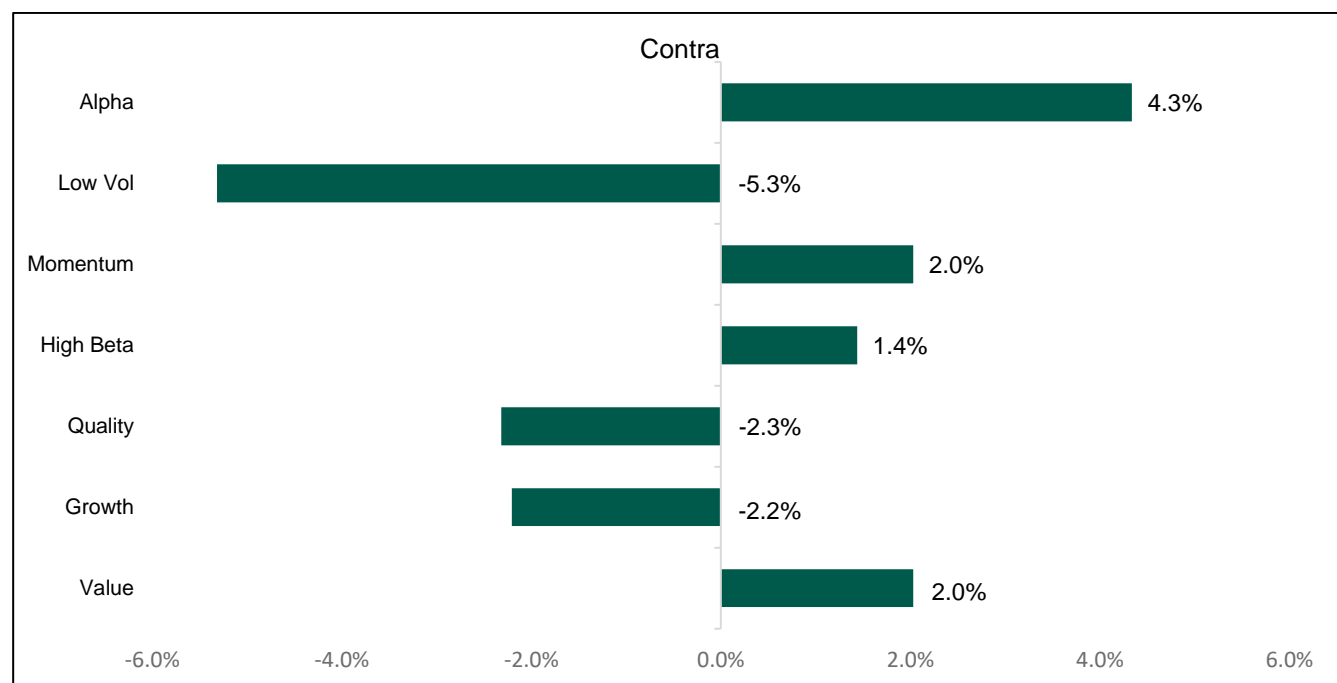
## Top 10 Holdings

Scrip Name	Market Cap (Cr)	Weight
Power Grid Corp Of India	2,54,976	5.5%
Thomas Cook (India) Ltd	8,290	5.4%
State Bank Of India	5,72,692	5.0%
ITC Ltd	5,37,538	5.0%
Indian Hotels Co Ltd	72,118	4.7%
Indus Towers Ltd	59,383	4.4%
Hindustan Petroleum Corp	76,467	4.4%
KDDL Ltd	3,436	4.3%
CIE Automotive India Ltd	18,832	4.2%
Mahindra & Mahindra Ltd	2,14,534	4.1%

## Portfolio Characteristics

	Contra
Number of constituents	25
Mcap Largest (Cr)	7,24,016
Mcap Smallest (Cr)	3,436
Mcap Average (Cr)	1,53,476
Mcap Median (Cr)	72,118

## Factor Box



The Factor Box provides relative factor exposure vis-à-vis a given benchmark. For instance, if the Growth factor exposure in a portfolio is 23% and the Growth factor exposure of the Benchmark is 20%, it indicates that your portfolio is "Overweight" on Growth with respect to the benchmark. A positive Value in the above Factor represents that the given portfolio is Overweight in the factor with respect to the benchmark. Similarly, a negative value would represent that the given portfolio is underweight in the factor with respect to the benchmark.

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