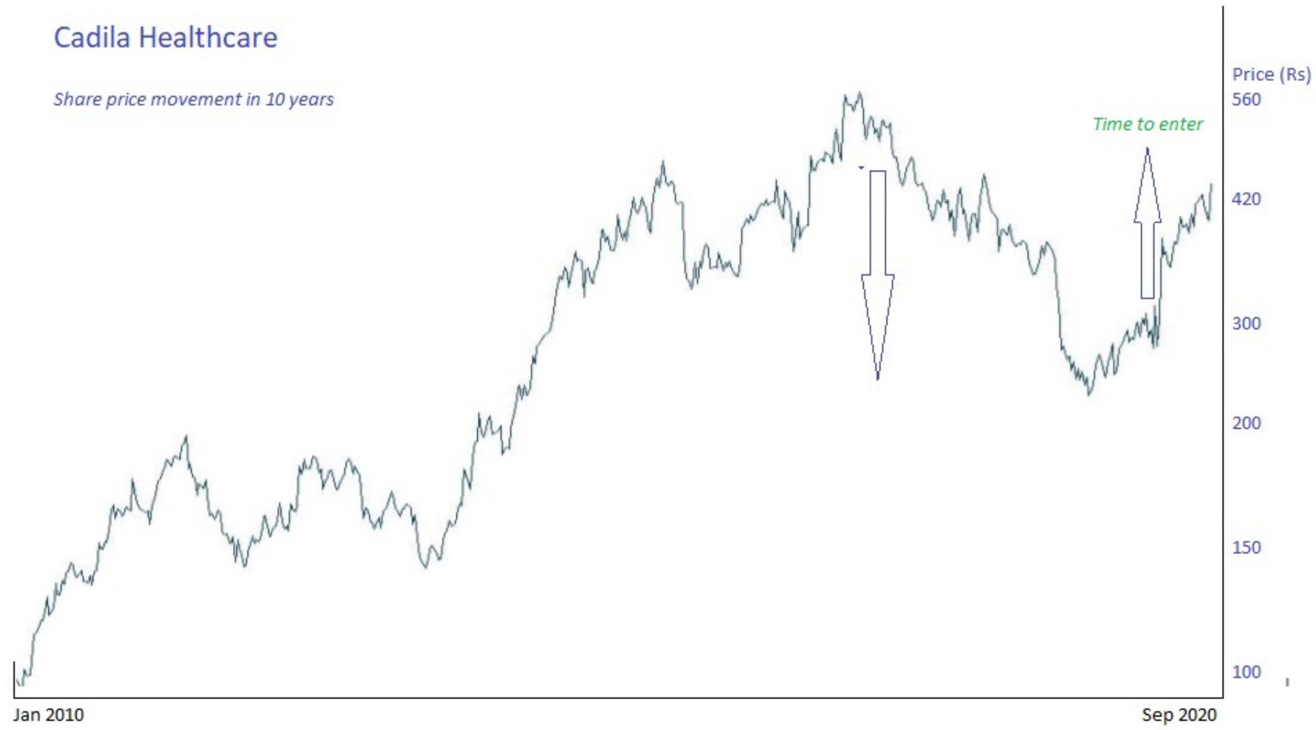
Cadila Healthcare: Strongest rally in 3 years signifies a turnaround

Cadila Healthcare has been seeing the strongest rally in recent times which clearly indicates a structural transformation. Time to enter!

Stable earnings visibility, least stressed balance sheets, healthy free cash flows and ability to deliver products at the time of crisis are some key attributes of Indian pharma.



Over the last few quarters, most players are recalibrating CAPEX and R&D spend in order to optimise capital utilisation. The current situation, underpinned by Covid-19 pandemic and its negative impact on most sectors, further strengthens the argument for investment in pharma.

While the Q1 performances of most pharma companies have been skewed, H2 should reflect the normalised trend.

Technically, the Pharma index has registered a structural turnaround on long term charts. At the current juncture, Cadila Healthcare and Caplin Point Laboratories seem to be well placed in terms of a favourable risk-reward set-up from a medium-term perspective.

The pharma sector has been relatively outperforming over the past couple of months after witnessing a structural turnaround off March 2020 lows, signalling a reversal of five-year-long downtrend.

o In the pharma space, Cadila Healthcare has been relatively underperforming. However, currently, it has been seeing a faster pace of retracement as it retraced past five week's decline (Rs 412-358) in just a single week, signalling an acceleration of upward momentum, auguring well for the next leg of up. Structurally, the stock has witnessed strongest up move since CY17 as a current up move off March low of Rs 202 (108%) is stronger than CY16-17 rally (90%). The elongated rally signifies structural
turnaround.

o It appears the stock has strong support at Rs 372 as it is 80% retracement of ongoing up move (Rs 420-358), at Rs 370. Hence, after a faster retracement, temporary breather from here on should be used as incremental buying opportunity.

o The stock may form a higher base and gradually head towards Rs 485 levels in coming months as it the 80% retracement of 2017-19 decline (Rs 560-206) placed at Rs 488.

Cadila Healthcare is one of the old generation family-owned pedigree companies which, after establishing a strong base in domestic formulations, shifted focus to the exports markets

• US (44% of FY20 revenues) grew at ~12% CAGR in FY16-20 backed by aggressive filings, product launches. Launch of authorised generics also contributed to overall growth. US pipeline (cumulative) consists of 390+ filed ANDAs, 95 pending final approvals. However, resurfacing of cGMP issues at Moraiya, an imminent slowdown in the base are main near term headwinds. We expect US sales to grow at ~9% CAGR in FY20-22E to Rs 7426 crore

• With a market share of 4.1%, Cadila Healthcare is the fifth-largest player in the domestic formulations market, as per AIOCD June 2020. The acute: chronic: subchronic ratio for the company is 53:31:16. Domestic formulation grew at a CAGR of 5.7% in FY16-20 backed by new launches and acquisition of Biochem. Recently, the company optically initiated a restructuring of business by rationalising slow-moving SKUs. We expect Indian formulations to grow at a CAGR of ~9% in FY20-22E to Rs 4432 crore.

• On the US front, the company plans to venture into complex injectables (45 filed ANDAs + 14 in-licensed products), which is likely to provide meaningful traction from FY23-24 onwards. Similarly, the addition of biosimilars (like Trastuzumab, Adalimumab, Pegfilgrastim, Bevacizumab, etc.) for Emerging markets (like LatAm, MENA markets and South East Asia) are expected to provide growth impetus, going ahead. The wellness segment performance hinges upon the company’s marketing & distribution prowess besides effective product positioning. India formulations business, after recent restructuring, is likely to stabilise. Both wellness, India formulations are likely to deliver steady growth in FY22. Overall, balance sheet reduction, Moraiya warning letter resolution, US base business performance in tough times are some important aspects to watch.

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