

Results Update

Hester Biosciences Ltd

Bloomberg Code: HBIO IN

India Research - Stock Broking

BUY

High-margin Large Animal Vaccines Sales to Boost Both Revenues and Operating Leverage

Domestic Brucella and PPR Vaccines Sales Drive Profitability: A surprise and significant jump in domestic Large Animal Vaccines (LAV) sales - primarily Brucella vaccine and to smaller degree PPR vaccines - have led to considerable expansion in gross margin and EBITDA margin. LAV sales have increased from Rs.2.2 Mn in Q2FY17 to Rs.56.2 Mn in Q2FY18. During Q1FY18 LAV sales were Rs.4.9 Mn. Both Brucella and PPR sales during the quarter are attributed to tender orders from about 10 state governments. Management believes that these orders are not only sustainable but will also increase in size in the future as more states start participating in issuing tenders. Competition is expected to be limited with about 2 firms for Brucella vaccine and about 3 firms for PPR vaccine. Management believes that margins may expand further with rising LAV sales - both domestic and exports.

Slow Traction in PPR Exports from Nepal But is Expected to Ramp-up by End of FY18E and During FY19E: Nepal plant has required the approvals from African Quality Control Lab, this enables the firm to participate and compete in the FAO tenders process. Tendering by FAO has been slow leading to smaller PPR sales. Management says that they would quote PPR vaccine at a price higher than that in India and expects to be the lowest price bid. During H1FY18, Nepal facility had sales of Rs.19.4 Mn and a net loss of about Rs.19 Mn. Management expects that in the near-to-mid term, PPR tendering would pick-up and that the financial health of Nepal plant would turn around.

Valuation and Outlook

We are introducing FY19E financials in this report. At CMP of Rs.1162, HBL is currently trading at P/E of 18.1x based on FY19E EPS of Rs.64.4. Rise in high-margin LAV sales would lead to higher operating leverage, clearly visible in 813 bps expansion in EBITDA margin. We believe that the company is well-poised for significant growth in the future. We, thus, reiterate a **“BUY”** recommendation with Rs.1417 target price revised upwards based on 22x FY19E EPS of Rs.64.4. The target of Rs.1417 represents a potential upside of 22%.

Exhibit 1: Valuation Summary

YE Mar (Rs. Mn)	FY15	FY16	FY17	FY18E	FY19E
Net Sales	900	1009	1230	1591	1980
EBITDA	241	326	409	663	884
EBITDA Margin (%)	26.8	32.3	33.2	41.7	44.7
Adj. Net Profit	119	189	234	407	548
EPS (Rs.)	14.0	22.2	27.6	47.8	64.4
RoE (%)	14.8	19.9	20.3	28.8	30.3
PE (x)	33.5	22.7	27.7	24.3	18.1

Source: Company, Karvy Research, *Represents multiples for FY15, FY16 & FY17 are based on historic market price

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Recommendation (Rs.)

CMP (as on Nov 30, 2017)	1162
Target Price	1417
Previous Target Price	873
Upside (%)	22

Stock Information

Mkt Cap (Rs.mn/US\$ mn)	9740 / 151
52-wk High/Low (Rs.)	1278 / 681
3M Avg. daily volume	9635
Beta (5-yr)	1.4
Sensex/Nifty	33149 / 10227
O/S Shares(mn)	8.5
Face Value (Rs.)	10.0

Shareholding Pattern (%)

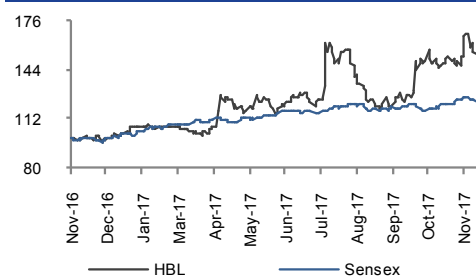
Promoters	54.1
FIIIs	0.9
DIIIs	1.2
Others	43.9

Stock Performance (%)

	1M	3M	6M	12M
Absolute	11	34	34	63
Relative to Sensex	10	27	27	37

Source: Bloomberg

Relative Performance*



Source: Bloomberg; *Index 100

Earnings Revision (%)

YE Mar	FY18E
Sales (%)	↓ (7.5)
EBITDA (%)	↑ 4.1
PAT (%)	↑ 9.6

Source: Karvy Research

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Exhibit 2: Quarterly performance comparison

YE Mar (Rs. Mn)	Q2FY18	Q1FY18	QoQ (%)	Q2FY17	YoY (%)	H1FY18	H1FY17	YoY (%)
Sales	385	290	32.5	296	29.9	675	598	13.0
Operating Expenses	234	183	28.1	204	14.6	417	399	4.6
EBITDA	151	108	40.0	92	63.9	258	199	29.8
Depreciation	13	14	(4.1)	13	(1.4)	27	26	2.7
Interest	4	6	(42.9)	9	(59.8)	10	17	(41.6)
Other Income	6	6	13.7	1	466.7	12	4	165.0
PBT	140	93	50.4	71	97.9	233	161	45.3
Tax	52	31	64.9	11	362.9	83	41	102.7
Adjusted PAT	89	62	43.0	60	48.3	150	120	25.7
EBITDA Margin (%)	39.2	37.1	209 bps	31.0	813 bps	38.3	33.3	495 bps
EBIT Margin (%)	37.3	34.2	313 bps	26.9	1048 bps	36.0	29.6	635 bps
Net Profit Margin (%)	23.0	21.3	170 bps	20.1	286 bps	22.3	20.0	225 bps

Source: Company, Karvy Research

Exhibit 3: Segment-wise Financials

YE Mar (Rs. Mn)	Q2FY18	Q1FY18	QoQ (%)	Q2FY17	YoY (%)	H1FY18	H1FY17	YoY (%)
Segment-wise Revenue								
Poultry	299	267	12.1	270.5	10.7	566	556	2.0
Large Animal	85	23	266.1	31.2	173.9	109	53	104.0
Segment-wise EBIT								
Poultry	99	97	1.5	77	27.8	196	174	12.5
Large Animal	45	2	1996.7	3	1551.3	47	4	1190.4
Segment-wise EBIT Margin (%)								
Poultry	33.0	36.4	(344) bps	28.5	443 bps	34.6	31.3	323 bps
Large Animal	52.8	9.2	4,355 bps	8.8	4,401 bps	43.4	6.9	3,655 bps

Source: Company, Karvy Research

Key takeaways from concall

- Hester Biosciences Ltd (HBL) has developed a new thermostable Newcastle disease vaccine for poultry. Newcastle is the most common disease in poultry worldwide and this thermostable vaccine is being given mainly to the backyard poultry farmers.
- Company has embarked on a project in three states (Orissa, Chhattisgarh, and Jharkhand) in India to immunize the backyard poultry.
- Backyard poultry project gives the company immense visibility as well as goodwill in rural India. In the long-run, management expects to use the resulting distribution network to supply other poultry health products like dewormer.
- During HY18, HBL has spent Rs.83.6 Mn in capex and management believes that additional capex during H2FY18 would be about Rs.50 Mn to Rs.60 Mn.
- HBL has diverted some orders from private companies due to unexpected large orders from state governments for LAV and some ability related to completing orders in time. Management is addressing this through both extensive planning and some additional capex.
- The company is currently conducting a market survey and feasibility study to setup a manufacturing facility in Tanzania for manufacturing vaccines for Africa-specific diseases. The estimated cost of the facility is about \$12 Mn to \$15 Mn.
- Registrations to sell poultry vaccines have been completed in Egypt, Nigeria, Ethiopia, Malawi, Vietnam and Cambodia.

Exhibit 4: Revised Earnings Estimates

YE Mar (Rs. Mn)	FY18E			FY19E	Comments
	Earlier	Revised	% change	Introducing	
Net Sales	1721	1591	(7.5)	1980	Delay in PPR export sales, but margins expanded significantly due to jump in Brucella vaccine sales.
EBITDA	637	663	4.1	884	
EBITDA margin (%)	37.0	41.7	465 bps	44.7	
Adj. PAT	371	407	9.6	548	
EPS (Rs.)	43.6	47.8	9.6	64.4	

Source: Karvy Research

Key Risks

- HBL not able to win/execute Brucella and PPR vaccines tenders in India and/or PPR vaccine tenders in Africa.
- Intense competition in both Brucella vaccines and PPR vaccines leading to significant price erosion.
- Unexpected/Unforeseen problems occurring at the Nepal facility.

Financials

Exhibit 5: Income Statement

YE Mar (Rs. Mn)	FY15	FY16	FY17	FY18E	FY19E
Revenues	900	1009	1230	1591	1980
Growth (%)	30.4	12.1	22.0	29.3	24.4
Operating Expenses	659	683	822	929	1096
EBITDA	241	326	409	663	884
Growth (%)	(1.3)	35.1	25.4	62.2	33.4
Depreciation & Amortization	59	58	70	89	94
Other Income	4	12	4	4	4
EBIT	186	280	343	578	794
Interest Expenses	48	37	35	41	44
PBT	164	243	308	538	750
Tax	41	63	73	127	178
Adjusted PAT	119	189	234	407	548
Growth (%)	25.7	58.9	24.2	73.4	34.7

Source: Company, Karvy Research

Exhibit 6: Balance Sheet

YE Mar (Rs. Mn)	FY15	FY16	FY17	FY18E	FY19E
Cash & Cash Equivalents	81	53	120	410	765
Sundry Debtors	184	262	265	343	427
Inventory	291	336	334	382	436
Loans & Advances	128	126	160	124	141
Investments	3	1	0	0	0
Gross Block	977	1072	1517	1667	1867
Net Block	592	646	1026	1088	1193
CWIP	318	365	213	289	200
Miscellaneous	0	70	63	72	72
Total Assets	1597	1858	2181	2708	3234
Current Liabilities & Provisions	150	172	221	277	348
Debt	550	541	629	757	752
Other Liabilities	59	82	89	96	96
Total Liabilities	759	795	939	1129	1195
Shareholders Equity	85	85	85	85	85
Reserves & Surplus	739	932	1111	1444	1880
Total Network	824	1017	1196	1529	1965
Minority Interest	15	46	46	49	74
Total Network & Liabilities	1597	1858	2181	2708	3234

Source: Company, Karvy Research

Exhibit 7: Cash Flow Statement

YE Mar (Rs. Mn)	FY15	FY16	FY17	FY18E	FY19E
PBT	164	248	308	538	750
Depreciation	59	58	70	89	94
Interest	48	37	35	41	44
Tax Paid	(55)	(60)	(71)	(127)	(178)
Inc/dec in Net WC	41	(94)	1	(36)	(84)
Other Income	1	1	1	4	4
Other non cash items	34	58	75	89	94
Cash flow from operating activities	232	188	348	500	623
Inc/dec in capital expenditure	(76)	(139)	(302)	(150)	(200)
Inc/dec in investments	(6)	1	(2)	0	0
Others	(147)	5	3	(72)	93
Cash flow from investing activities	(228)	(133)	(302)	(222)	(107)
Inc/dec in borrowings	85	23	88	127	(5)
Issuance of equity	0	14	7	0	0
Dividend paid	(20)	(37)	(16)	(73)	(112)
Interest paid	(48)	(37)	(35)	(41)	(44)
Others	5	(29)	(26)	0	0
Cash flow from financing activities	22	(67)	18	13	(161)
Net change in cash	26	(11)	64	291	355

Source: Company, Karvy Research

Exhibit 8: Key Ratios

YE Mar	FY15	FY16	FY17	FY18E	FY19E
EBITDA Margin (%)	26.8	32.3	33.2	41.7	44.7
EBIT Margin (%)	20.6	27.8	27.9	36.3	40.1
Net Profit Margin (%)	13.2	18.7	19.1	25.6	27.7
Dividend Payout Ratio (%)	22.2	18.5	19.2	15.0	17.0
Net Debt/Equity (x)	0.56	0.46	0.41	0.22	(0.01)
RoE (%)	14.8	19.9	20.3	28.8	30.3
RoCE (%)	14.3	18.7	19.7	27.5	31.0

Source: Company, Karvy Research

Exhibit 9: Valuation Parameters

YE Mar	FY15	FY16	FY17	FY18E	FY19E
EPS (Rs.)	14.0	22.2	27.6	47.8	64.4
DPS (Rs.)	3.1	4.1	5.3	7.2	10.9
BVPS (Rs.)	98.6	125.0	146.0	185.6	239.7
PE (x)	33.5	22.7	27.7	24.3	18.1
P/BV (x)	4.7	4.0	5.2	6.3	4.8
EV/EBITDA (x)	18.5	14.8	17.2	15.5	11.2
EV/Sales (x)	5.0	4.8	5.7	6.5	5.0

Source: Company, Karvy Research, *Represents multiples for FY15, FY16 & FY17 are based on historic market price

Stock Ratings		Absolute Returns
Buy	:	> 15%
Hold	:	5-15%
Sell	:	< 5%

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