

Company Report

Tuesday, October 8, 2024

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Securities

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Coverage Initiation

COMPANY UPDATE

Haleon Pakistan Limited (HALEON)

Pharmaceuticals

| | |
|------------------------|------------|
| Recommendation | BUY |
| Target Price: Jun-25 | 787 |
| Last Closing: 3-Oct-24 | 586 |
| Upside (%): | 34% |
| Valuation Methodology: | DCF |

Market Data

| | | | | |
|------------------------|------------|------------|------------|------------|
| Bloomberg Tkr. | HALEON PA | | | |
| Shares (mn) | 117.05 | | | |
| Free Float Shares (mn) | 15.6 | | | |
| Free Float Shares (%) | 13.4% | | | |
| Market Cap (PKRbn) | 71.4 | | | |
| Market Cap (USDmn) | 257.2 | | | |
| Exchange | KSE-100 | | | |
| Price info. | 01M | 03M | 09M | 12M |
| Abs. Return | 42% | 89% | 3.1x | 2.9x |
| Low | 401 | 248 | 161 | 147 |
| High | 587 | 587 | 587 | 587 |

Key Company Financials

Period End: Dec

| PKRbn | CY23A | CY24E | CY25E | CY26E |
|---------------|--------|--------|--------|--------|
| Total Revenue | 31,610 | 42,284 | 51,372 | 62,421 |
| Net Income | 0,996 | 3,750 | 4,770 | 6,046 |
| EPS (PKR) | 8.51 | 32.03 | 40.75 | 51.65 |
| DPS (PKR) | 0.0 | 10.0 | 10.0 | 15.0 |
| Total Assets | 18,245 | 20,046 | 22,748 | 26,718 |
| Total Equity | 8,023 | 10,654 | 14,477 | 19,122 |

Key Financial Ratios

| | | | | |
|---------|------|------|------|------|
| ROE (%) | 13% | 41% | 40% | 38% |
| P/E (x) | 68.9 | 18.0 | 13.7 | 10.7 |
| P/B (x) | 8.9 | 6.7 | 4.9 | 3.7 |
| DY (%) | - | 2% | 2% | 3% |

Source: Bloomberg, CapitalStake, PSX, Company Financials, IGI Research

IGI Research

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Pharmaceuticals

HALEON: Thriving on Regulatory and Macroeconomic Tailwinds

- We initiate coverage on HALEON with a buy rating and target price of PKR 787/share offering 34% upside from last close. Haleon Pakistan, established in 2022 following a global demerger from GlaxoSmithKline, is recognized as a prominent player in the country's consumer healthcare industry. Before this demerger, the business operated under the name GlaxoSmithKline Consumer Health. The company has a long history of developing well-known brands with a strong legacy, including Panadol, CAC-1000 Plus, and Sensodyne.
- We estimate HALEON earnings for next 5 years to post 26% CAGR reaching PKR 10.0bn compared to the last reported earnings of PKR 1.0bn.
- Using DCF, we have a 'BUY' rating on HALEON with a Jun-25 target price of PKR 787/share offering ≈ 34% upside from the last closing price of PKR 586/share. The Company trades at CY24/25 P/E of 18.0/13.7 with 2% dividend yield.

Initiating Coverage on Haleon Pakistan Limited (HALEON) with "BUY" Rating

We initiate coverage on HALEON with a buy rating and target price of PKR 787/share offering 34% upside from last close. Haleon Pakistan, established in 2022 following a global demerger from GlaxoSmithKline, is recognized as a prominent player in the country's consumer healthcare industry. Before this demerger, the business operated under the name GlaxoSmithKline Consumer Health. The company has a long history of developing well-known brands with a strong legacy, including Panadol, CAC-1000 Plus, and Sensodyne. With its advanced production facility, the company has consistently expanded its market presence across various categories in which it operates.

We base our investment thesis on a) recent deregulation of non-essential drug prices by DRAP, b) Special approvals by DRAP for hike in Paracetamol prices, c) Stable exchange rates, d) Debt-free balance sheet, and e) Capacity expansion and addition of new products into the portfolio.

Recommendation: We have a 'BUY' rating on HALEON with a Jun-25 target price of PKR 787/share offering a ~34% upside from the last closing price of PKR 586/share (7-Oct-24). The Company is currently trading at CY24/25 P/E of 18.7/14.2 and offers a dividend yield of 2%.

Key Catalyst: Key catalyst include a) Regulations related to counterfeit products, b) potential deregulation of essential drugs prices, and c) More than expected increase in essential drug prices.

Key Risk: Key risk include a) more than expected PKR depreciation, b) Geopolitical tensions, c) further increase in availability of counterfeit products.

Investment Thesis

1. Regulatory Tailwinds

Deregulation of non-essential drugs prices:

In February 2024, DRAP deregulated the prices of non-essential drugs. Previously, pharmaceutical companies were allowed to raise prices annually, capped at the lower of 10% of the CPI or 10%. With the removal of this policy, companies involved in non-essential drugs now have a greater pricing flexibility, providing them with a competitive advantage. As of June 2024, around 15% of Haleon Pakistan’s sales mix consisted of non-essential drugs. This indicates that approximately 15% of their total sales would be free from any regulation, and the company would have autonomy to fix the prices of those drugs.

Special approvals for increase in Paracetamol Prices by DRAP:

Haleon Pakistan, the manufacturer of Panadol, a drug listed under the National Essential Medicine List (NEML). According to our market research and analysis, the price of Panadol has surged by approximately 45%, with four hikes occurring between November 2022 and September 2024. The current MRP for a box of Panadol 500mg (200 tablets) stands at PKR 704.88. These price increases are largely due to the shortage of Panadol in 2022 and early 2023, which fueled black market activity. Additionally, the manufacturers were unable to secure price adjustment to offset rising production costs caused by depreciating rupee and escalating inflation. The last 4 price increases for Panadol seem to be very positive for the company as they have been properly able to pass on all the cost impact to the customers and have secured better gross margins. It is important to note that Panadol contributes more than ~52% of the total sales of Haleon Pakistan.

Exhibit: Haleon Sales Mix

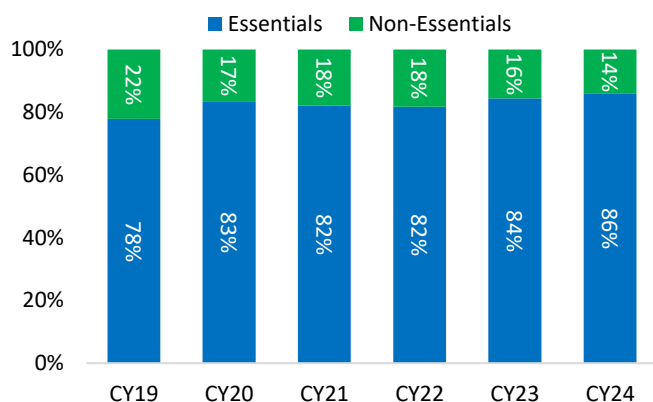


Exhibit: Imported vs local APIs

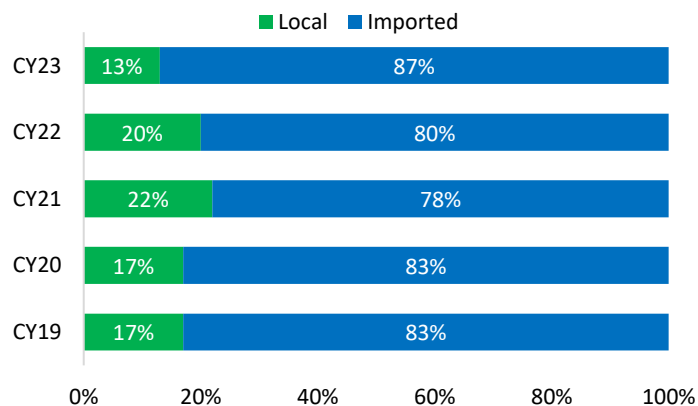


Exhibit: Panadol and CAC 1000 Plus: Haleon's Bestsellers

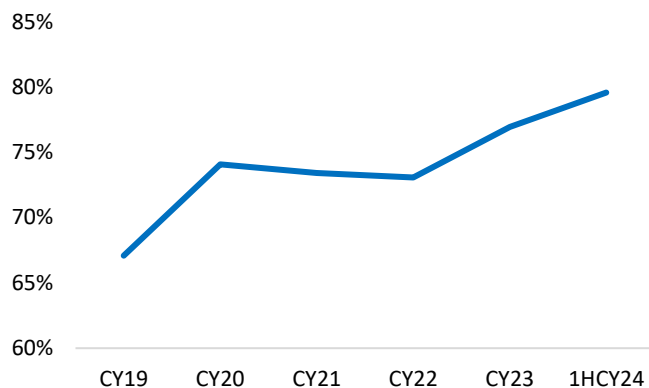
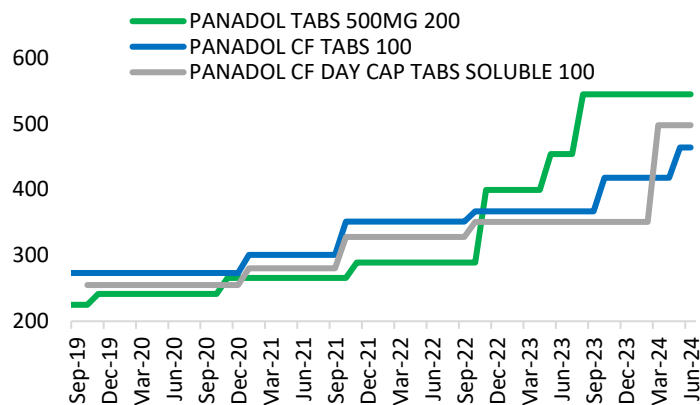


Exhibit: Panadol Prices



Source: IQVIA, Company Accounts, IGI Research

2. Stable Exchange Rates

The country's improving economic conditions and the buildup of foreign exchange reserves have kept the rupee stable throughout the year. The stability is crucial for the pharmaceutical sector, which is heavily reliant on imports, as it minimizes exchange rate losses. Haleon Pakistan in particular depends on Active Pharmaceutical Ingredients (APIs) for drug production, with around 87% of its raw material sourced from abroad. As a result, the stability of the exchange rate is vital for the company, and with the rupee holding steady, Haleon Pakistan is in a very strong position.

Exhibit: Haleon leads Pakistan's pain care market

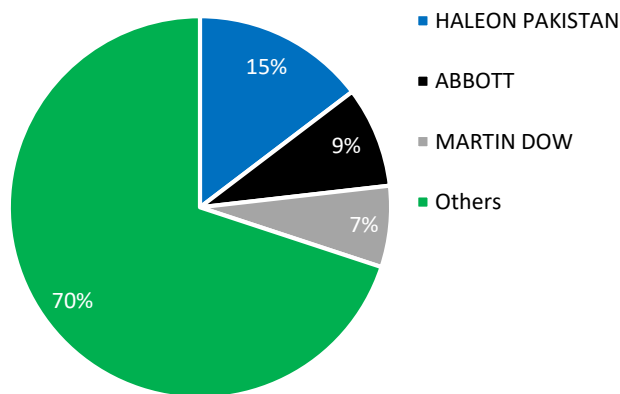
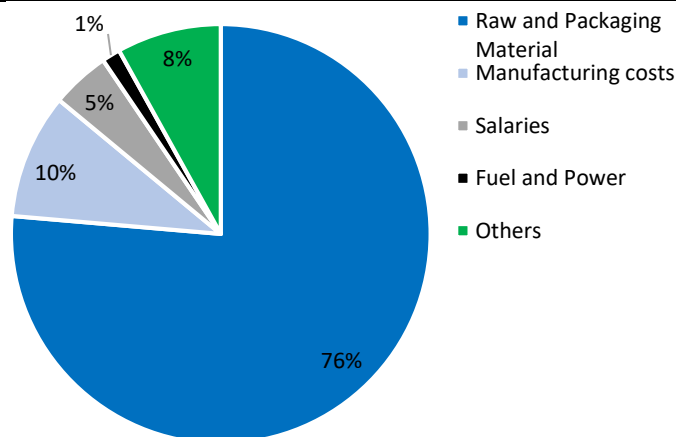


Exhibit: COGS Decomposition



Source: IQVIA, Company Accounts, IGI Research

3. Debt-free Balance sheet

Haleon Pakistan doesn't have any long-term or short-term loans on its balance sheet, which makes it even good buy, as they don't have any significant finance cost to pay.

4. Capacity Expansion and addition of new products into the portfolio



As per the 2023 annual report of the Company, Haleon Pakistan’s Jamshoro plant secured financial approval for £9.8mn in capital expenditure (CAPEX) to bring the production of Panadol Extra and Panadol Plain tablets in-house. This investment is aimed at strengthening the company’s foothold in the Pakistani market by enhancing local manufacturing capabilities. Additionally, the plant has plans to introduce three new products this year: locally manufactured Panadol Extend tablets, Hydrozole Cream, and CAC Kids Effervescent Tablets. These new product launches are part of the Company’s broader strategy to expand its portfolio and meet the growing demand in the local market. The move underscores Haleon’s commitment to improving its operational capacity and increasing its product offerings in Pakistan.

5. Strong Future Earnings Growth

Haleon Pakistan has posted negative earnings growth at 3yr CAGR (CY21-23) of -22% owing to the pricing related regulations and exchange losses. Going forward, we estimate the Company’s earnings to register 26% CAGR (CY24-28) reaching PKR 10.0bn by CY28 compared to PKR 1.0bn in CY23.

Valuation

Using DCF, we have a 'BUY' rating on HALEON with a Jun-25 target price of PKR 787/share offering a ~34% upside from the last closing price of PKR 586/share (7-Oct-24). HALEON offers CY25E FCF yield of ~18%.

We have determined our target price using Discounted Cash Flow (DCF) valuations with a WACC of 21%, Cost of Equity of 21.3% and a terminal growth rate assumed at 3% based on cash flows projected until CY30. Our calculation includes a risk-free rate of 15%, a beta of 1.05, and an equity risk premium of 6%.

Trading at significant discount to historic P/E

The company is currently trading at 2024F P/E of 21.49x significantly discounted to historic average of 23.30x.

Exhibit: Relative Price Performance

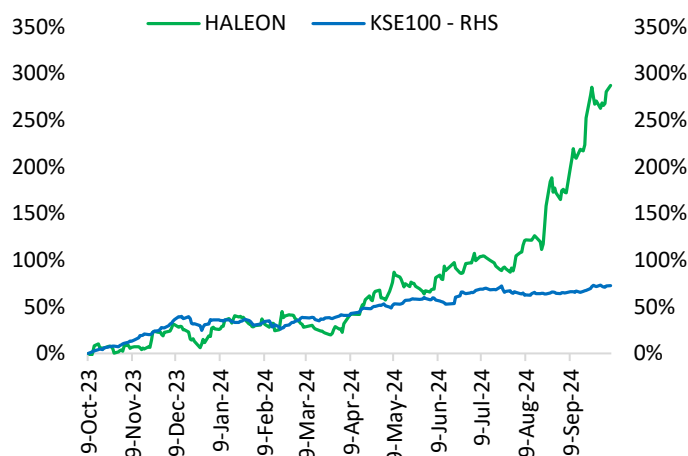
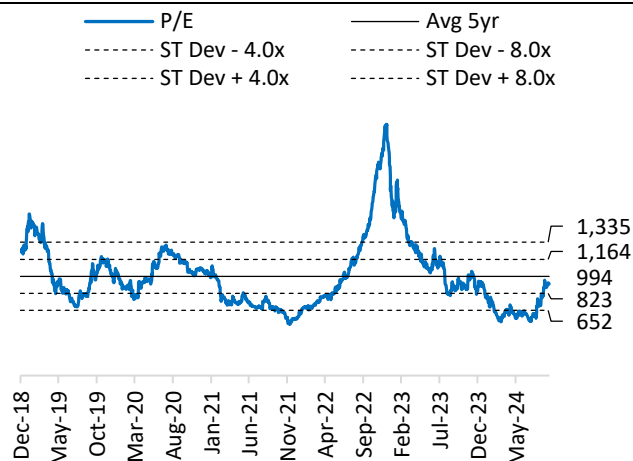


Exhibit: Historical P/E & Standard Deviation



Source: PSX, Company Accounts, IGI Research

Key Catalyst

1. **Tackling counterfeit drugs through regulation for sector growth:** The rampant availability of counterfeit drugs poses a significant threat to legitimate pharmaceutical companies, undermining their market share and eroding consumer trust while compromising patient safety. Implementing stringent regulatory measures to restrict the distribution of these counterfeit products can serve as a crucial catalyst for the industry. By cracking down on grey market activities, regulatory authorities can create a safer and more transparent environment that enables legitimate companies to reclaim lost market share and potentially expand their customer base.

2. **Talks about deregulation of Essential drug prices on the cards:** There are wide rumors that government is also considering the partial deregulation of Essential drugs. Under the Prime Minister Shahbaz Sharif's directives the Ministry of National Health Services, Regulation and Coordination (NHRS&C) is considering to relieve DRAP of its price setting duties and a new federal body will be formed which will regulate the prices of drugs.
3. **More than expected increase in essential drug prices:** For our forecast, we have assumed a price increase for all essential drugs capped at either 7% of 70% of the CPI for CY25 and beyond. However, based on the trends observed over the last two years, Haleon Pakistan has managed to secure price increases for Panadol that exceed regulatory limits. If this trend continues, we can expect margins to improve, leading to even stronger earnings.

Risk to Rating

1. **More than expected PKR depreciation:** Haleon Pakistan's profitability is heavily influenced by exchange rates due to its reliance on imported raw materials. The significant volatility of the Pakistani rupee during 2021-22 impacted earnings across the pharmaceutical sector. While the rupee has remained stable in 2024, enabling earnings growth, the risk of future currency fluctuations persists. This is due to Pakistan's fragile political landscape and dependence on foreign exchange reserves, primarily funded by external lenders like the IMF. Political instability can stall this support, depleting reserves and putting downward pressure on the rupee, which threatens import-dependent industries like pharmaceuticals.
2. **Geopolitical tensions:** As mentioned earlier in the report, Haleon Pakistan's reliance on imported raw materials makes it vulnerable to global geopolitical tensions, which can severely affect the company's performance. These tensions often disrupt supply chains, delaying the import of essential Active Pharmaceutical Ingredients (APIs). Pakistan primarily sources these APIs from the USA, India, and China. Due to trade restrictions with India, APIs from there must be imported via alternative routes, adding further complexity. Any disruptions in the supply chain can lead to delays in raw material imports, causing operational inefficiencies and hindering the company's ability to meet market demand. This creates significant challenges in maintaining smooth operations and fulfilling customer expectations.
3. **Further increase in availability of counterfeit products:** Counterfeit products threaten companies like Haleon Pakistan by eroding trust, market share, and public safety. These fakes, sold at lower prices, divert customers from genuine products and damage brand reputations. Any rise in counterfeits would further harm market share and negatively impact the listed pharmaceutical sector.

Financial Summary

Haleon Pakistan Limited (HALEON)

Current Price (PKR): 586
Target Price (PKR): 787
Upside: 34%
Recommendation: BUY

| PKRbn | CY20A | CY21A | CY22A | CY23A | CY24E | CY25E | CY26E | PKRbn | CY20A | CY21A | CY22A | CY23A | CY24E | CY25E | CY26E |
|-------------------------|--------|--------|--------|--------|--------|--------|--------|-----------------------------------|-------|-------|--------|-------|-------|-------|-------|
| Income Statement | | | | | | | | Per Share | | | | | | | |
| Net Sales | 19,846 | 24,163 | 27,507 | 31,610 | 42,284 | 51,372 | 62,421 | EPS | 10.8 | 18.2 | 2.8 | 8.5 | 32.5 | 42.7 | 54.7 |
| Gross Profit | 5,328 | 6,685 | 4,785 | 6,449 | 12,009 | 14,913 | 18,496 | DPS | 5.0 | - | - | - | 10.0 | 10.0 | 15.0 |
| Operating Profit | 1,940 | 3,006 | 1,063 | 1,631 | 6,198 | 8,142 | 10,605 | BVPS | 44.1 | 57.4 | 60.2 | 68.5 | 91.0 | 123.7 | 163.4 |
| EBITDA | 2,208 | 3,307 | 1,396 | 2,064 | 6,748 | 8,726 | 8,726 | Growth rates & Margins | | | | | | | |
| Finance Costs | 58 | 87 | 307 | 236 | 262 | 244 | 264 | Sales Gr. % | 0% | 22% | 14% | 15% | 34% | 21% | 22% |
| Profit Before Tax | 1,775 | 3,015 | 993 | 1,846 | 6,086 | 8,013 | 10,312 | EPS Gr. % | 0% | 69% | -85% | 206% | 282% | 31% | 28% |
| Taxation | 512 | 882 | 667 | 851 | 2,284 | 3,020 | 3,911 | Gross Margin | 27% | 28% | 17% | 20% | 28% | 29% | 30% |
| Profit After Tax | 1,263 | 2,133 | 325 | 996 | 3,802 | 4,993 | 6,401 | EBIT Margin | 10% | 12% | 4% | 5% | 15% | 16% | 17% |
| Balance Sheet | | | | | | | | Net Margin | 6% | 9% | 1% | 3% | 9% | 10% | 10% |
| Inventory | 2,902 | 3,916 | 4,529 | 5,415 | 5,910 | 7,030 | 8,365 | Valuation | | | | | | | |
| Receivables | 670 | 1,102 | 636 | 610 | 1,065 | 1,572 | 2,248 | P/E | 54.3x | 32.2x | 210.8x | 68.9x | 18.0x | 13.7x | 10.7x |
| Current Assets | 7,336 | 10,014 | 10,908 | 12,650 | 14,948 | 19,849 | 25,963 | DY | 1% | 0% | 0% | 0% | 2% | 2% | 3% |
| PP&E | 3,493 | 3,706 | 3,990 | 5,398 | 5,655 | 5,903 | 6,466 | P/B | 13.3x | 10.2x | 9.7x | 8.5x | 6.4x | 4.7x | 3.6x |
| Total Assets | 10,974 | 13,866 | 15,060 | 18,245 | 20,801 | 25,950 | 32,626 | Op. Cf Yld | 5% | 2% | 1% | 4% | 4% | 6% | 9% |
| Payables | 4,156 | 4,941 | 6,103 | 7,998 | 8,195 | 9,521 | 11,553 | ROE (%) | 26% | 36% | 5% | 13% | 41% | 40% | 38% |
| Total Liabilities | 5,810 | 7,151 | 8,018 | 10,222 | 10,226 | 11,552 | 13,584 | ROA (%) | 13% | 17% | 2% | 6% | 19% | 21% | 22% |
| Paid Up Capital | 1,171 | 1,171 | 1,171 | 1,171 | 1,171 | 1,171 | 1,171 | P/EBITDA | 31.1x | 20.7x | 49.1x | 33.2x | 10.2x | 7.9x | 7.9x |
| Total Equity | 5,164 | 6,715 | 7,042 | 8,023 | 10,654 | 14,477 | 19,122 | EV/EBITDA | 30.1x | 20.0x | 47.4x | 31.7x | 9.6x | 7.2x | 6.8x |

Source: PSX, Capital Stake, Company Accounts, Bloomberg, IGI Research

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Buy if target price on aforementioned security (ies) is more than 10%, from its last closing price(s)

Hold if target price on aforementioned security (ies) is in between -10% and 10%, from its last closing price(s)

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- Discounted Cash Flow (DCF)
- Reserve Based DCF
- Dividend Discount Model (DDM)
- Justified Price to Book
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