Twitter Thread by JST Investments

JST Investments
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Sequent is down 60% from its highs. Let's understand how their business is faring (by @AnishA_Moonka)

A thread ■■

1/ How do businesses happen? Do they just crop up the day when an entrepreneur thinks of it? Do they become bigger as the stock reaches new highs?

I guess, No. It takes time, It takes labor. Again, Will the ascension be smooth? Never.

The journey of Sequent in the last 5 yrs:

2/ Pre-FY15: Sequent was merely a commodity high volume low-value API player

Due to this intrapreneur's (Mr. Manish Gupta) efforts that we see Sequent as the only USFDA approved generic animal player from ■■

Behind the deals of Strides Agila plant & the Australian business.

3/ The transformation speaks volumes of how such a businessman thinks.

In 6yrs of existence, he has taken the unknown co. to be among the Top 20 in the world.

Now, he is taking a long shot to enter the Top 10 over the next decade (aka. Sequent 2.0); A tall task.

4/ If he is dreaming big & has executed in the past with industry tailwinds; the common question is why is the stock down by so much?

Probabilities: Investors went from a high probability of success to a low in months as multiple obstacles (short term?) hit the co.

5/ Again, It's not all hunky Dory.

While the rev growth is better than the industry, the co. has been struggling with margins for the last 2-3 quarters.

There are multiple obstacles & we will discuss them one by one.

6/ This quarter the gross margins have dropped to a 5yr low of 42.8%.

Particularly, the China power issue again (as I had discussed in my Laurus thread)

A sharp rise in input costs & given a B2B company; passing on takes a long time & is usually a difficult conversation.

7/ While it is visible that China+1 is playing out in the broad sense; the dependence on our neighbors is not going anytime soon, at least not for 2-3yrs

Such disruptions are a risk. Also, Higher inventories are an outcome (Higher Working capital)

Anyway, it will get passed on.

8/ Another risk that played out was of much lower orders in the API business especially Albendazole.

While the portfolio continues to grow in number & rev (up 25% in Q2FY22); the albendazole API degree by a lot leading to 10% regrowth overall

Stockpiling last year, hurt them.

9/ The biggest risk remains the Turkish Lira devaluation: Not even a forex expert knows

Sequent does get the benefit of a weaker currency to export (use Turkey as its supply base); however, the Turkey domestic biz gets hurt: In Q2 they grew 11% in cc but degree 7% in real terms.

10/ However, let's talk positives now

- Big Opportunity: $51B industry globally growing at 5-6% cagr
- Strong R&D efforts (Formulations & APIs) to drive the next leg of growth
- Major capacity expansion over FY22-23: focused on regulated markets

11/ - Top industry veterans induced into the board in the last year with a focus toward maximizing the Terminal value
- Optionality: CDMO & CMO contracts with Top 10 global Animal Healthcare cos.
- Capacity to suffer: Investing 200crs over the next 2 yrs in capability building.

12/ To summarise, there are multiple strands one can write on this niche industry with very strong economics once scale is reached. Think Zoetis.

However, I aspired to just clarify the misinterpretations. Let me know in the comments about your thoughts on Sequent 2.0
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End.

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