

INDUSTRY PHARMA

CMP (as on 06 Feb 2019) Rs 535

Target Price Rs 605

Nifty 11,062

Sensex 36,975

KEY STOCK DATA

Bloomberg CIPLA IN

No. of Shares (mn) 806

MCap (Rs bn) / (\$ mn) 431/6,023

6m avg traded value (Rs mn) 1,538

STOCK PERFORMANCE (%)

52 Week high / low Rs 678 / 484

3M 6M 12M

Absolute (%) 0.8 (16.1) (5.2)

Relative (%) (4.9) (14.2) (13.3)

SHAREHOLDING PATTERN (%)

Promoters 36.7

FIs & Local MFs 14.4

FPIs 25.2

Public & Others 23.7

Source : BSE

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US at a sweet spot

Cipla's reported an in-line quarter with revenue at Rs 40.1bn, up 2% YoY/ flat QoQ. EBITDA stood at Rs 7.1bn with margin at 17.7%, down 326bps YoY due to continued API cost inflation and falling prices in the tender business. PAT at Rs 3.3bn was down 17/12% YoY/QoQ (in-line).

With a ~9% QoQ jump in US revenues (US\$ 118mn), Cipla will most likely overshoot its guidance of US\$ 125mn US revenues in 4Q. The company has consistently launched niche products over the last few quarters, which has finally started reflecting in its US topline. As we had mentioned in our Dec-18 update, the ongoing issues related to supply constraints, geopolitical troubles in Yemen/ Iran and high inflation in API costs are temporary and have already been priced-in as the stock corrected ~22% from Rs 670 in Sep-18. Going ahead, resolution of these issues in 1-2 quarters along with further scale up in the US on the back of niche launches like gProventil and Tramadol will drive 14/33% rev/earnings CAGR (FY19-21E). The stock is trading at 24.6/18.3x FY20/21E EPS, a ~15% discount to its historical average. Maintain BUY with a TP of Rs 605 (22x Dec-20E EPS).

Financial Summary

Year Ending March (Rs bn)	3QFY19	3QFY18	YoY (%)	2QFY19	QoQ (%)	FY18	FY19E	FY20E	FY21E
Net Sales	40,075	39,138	2.4	40,119	(0.1)	152.19	159.65	182.37	208.11
EBITDA	7,077	8,187	(13.6)	7,022	0.8	28.26	27.14	33.75	42.05
APAT	3,322	4,005	(17.1)	3,771	(11.9)	14.94	13.25	17.53	23.51
Diluted EPS (Rs/sh)	4.1	5.0	(17.1)	4.7	(11.9)	18.6	16.5	21.8	29.2
P/E (x)						28.8	32.5	24.6	18.3
RoE (%)						11.2	9.0	10.9	13.1

Source: Company, HDFC sec Inst Research # Consolidated

Highlights of the quarter

- **The US:** US business' performance surprised positively, with revenue growing 31/12% YoY/QoQ to Rs 8.5bn. Growth was aided by product launches in the DTM business. This segment achieved post-R&D breakeven at the EBITDA level during the quarter. Exit revenue for 4Q should be at US\$ ~125mn, as guided by the management.
- **Other highlights:** (1) The domestic biz was flat YoY at Rs 15.9bn revenues owing to a weak acute season and high base. However, the company maintains its guidance of Rs 63-64bn India sales for FY19. (2) EU segment continued to perform well with revenue at Rs 1.9bn, up 11% YoY. This was driven by respiratory franchise expansion across key areas in EU. (3) EM segment was impacted due to geopolitical concerns in Yemen/ Iran. However, the biosimilars franchise continues to expand. (4) South Africa branded sales grew 7% YoY, despite slowdown in the overall market. (5) API segment grew 4% YoY. (6) R&D spend was at Rs 3bn for the quarter, ~7.5% of sales. (7) Tax rate was guided at ~28% for FY19.
- **Near-term outlook:** We expect the stock to recover post the recent correction. Niche US launches remain the key near-term triggers for the stock.

Revenue growth in the US was offset by decline in EM and the tender business

Gross margin declined ~130bps YoY/ QoQ due to API cost inflation and one-time low-margin sales in the tender business

R&D spend was at Rs 3bn, ~7.5% of sales

Tax rate should be at ~28% for the full year

Quarterly Financials Snapshot (Consolidated)

Particulars (Rs mn)	3QFY19	3QFY18	YoY (%)	2QFY19	QoQ (%)
Net Sales	40,075	39,138	2.4	40,119	(0.1)
Material Expenses	14,627	13,784	6.1	14,121	3.6
Employee Expenses	7,179	6,573	9.2	7,122	0.8
Other Operating Expenses	11,193	10,594	5.7	11,853	(5.6)
EBITDA	7,077	8,187	(13.6)	7,022	0.8
Depreciation	2,931	5,224	(43.9)	2,819	4.0
EBIT	4,145	2,963	39.9	4,203	(1.4)
Other Income	785	529		1,326	
Interest Cost	442	92		444	
PBT	4,489	3,401	32.0	5,085	(11.7)
Tax	1,257	(642)		1,424	
Share of profit/(loss) of associates	(10)	(9)		8	
Minority Interest	100	(29)		101	
RPAT	3,322	4,005	(17.1)	3,771	(11.9)

Source: Company, HDFC sec Inst Research

Margin Analysis

	3QFY19	3QFY18	YoY (bps)	2QFY19	QoQ (bps)
Material Expenses % Net Sales	36.5	35.2	128	35.2	130
Employee Expenses % Net Sales	17.9	16.8	112	17.8	16
Other Expenses % Net Sales	27.9	27.1	86	29.5	(162)
EBITDA Margin (%)	17.7	20.9	(326)	17.5	16
Tax Rate (%)	28.0	(18.9)	4,688	28.0	(0)
APAT Margin (%)	8.3	10.2	(194)	9.4	(111)

Source: Company, HDFC sec Inst Research

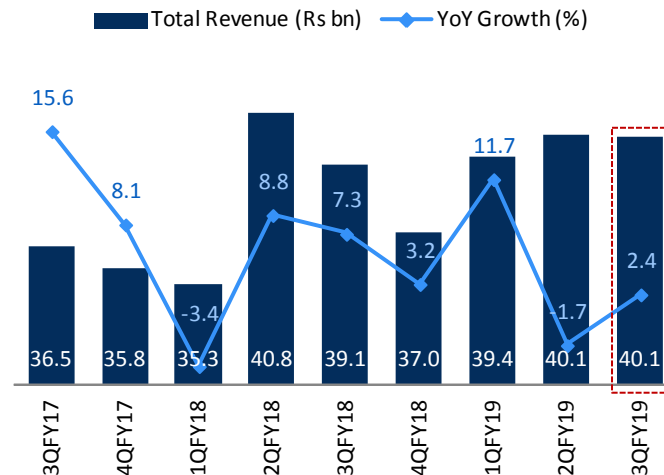
This was the second consecutive quarter with sequential growth in the US. Revenues were well above expectations, and the growth was aided by ramp up in the DTM segment

India business declined 1/4% YoY/QoQ due to a high base and weak acute season

EBITDA margin remained subdued due to lower gross margin and poor business mix

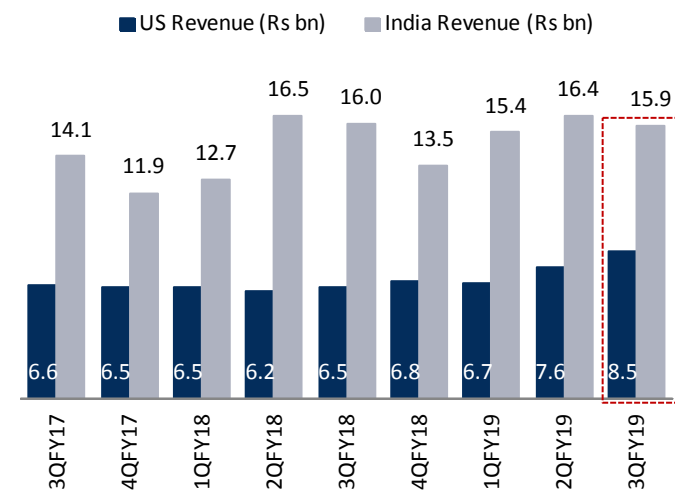
R&D spend is maintained along expected lines, at ~7.5% of sales. Advair trials are currently going on. Expenditure towards the specialty portfolio is limited to ~1.5% of sales

Topline Growth Supported By Scale-up In The US



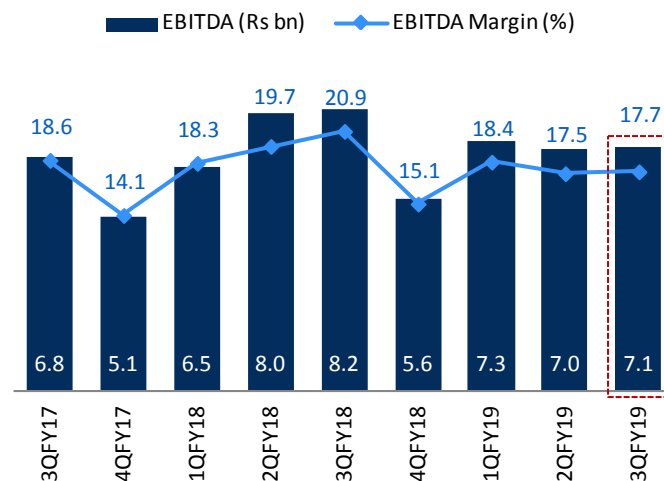
Source: Company, HDFC sec Inst Research

The Domestic Biz Was Flat YoY Due To A High Base



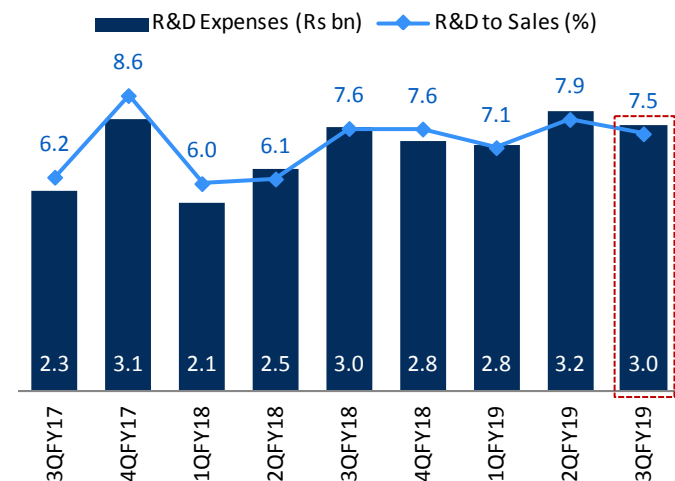
Source: Company, HDFC sec Inst Research

Margins To Improve As Ongoing Issues Resolve



Source: Company, HDFC sec Inst Research

R&D Spend Maintained Along Expected Lines



Source: Company, HDFC sec Inst Research

The US business achieved post-R&D breakeven at the EBITDA level.

Gained market share in Voltaren, now at ~35%.

The co. will file 2 respiratory products next year.

Invagen should report ~US\$ 200mn in revenue for FY19, impacted by higher price erosion.

Signed a deal for Bevacizumab and Trastuzumab biosimilars in multiple EM markets

Decline in EM reflects geopolitical issues and erosion of the SA tender biz

EU biz is doing well. Cipla continues to expand its respiratory franchise across key EU markets

Segmental Quarterly Performance

(Rs mn)	3QFY19	3QFY18	YoY (%)	2QFY19	QoQ (%)
India (Rx + Gx)	15,850	15,980	(0.8)	16,440	(3.6)
North America	8,490	6,490	30.8	7,580	12.0
South Africa	5,570	5,200	7.1	5,030	10.7
Europe	1,890	1,710	10.5	1,410	34.0
Emerging Markets	6,110	7,210	(15.3)	7,230	(15.5)
Global API	1,540	1,480	4.1	1,710	(9.9)
Others	640	1,060	(39.6)	720	(11.1)
Total	40,090	39,130	2.5	40,120	(0.1)

Source: HDFC sec Inst Research

Assumptions

Key segments (Rs mn)	FY17	FY18	FY19E	FY20E	FY21E
India	55,190	58,670	61,897	69,943	79,036
Growth (%)	9.9	6.3	5.5	13.0	13.0
North America	26,290	25,870	31,850	37,583	44,455
Growth (%)	24.9	(1.6)	23.1	18.0	18.3
South Africa	16,980	20,580	21,609	22,906	25,196
Growth (%)	8.2	21.2	5.0	6.0	10.0
Europe	6,200	6,230	6,220	6,967	8,026
Growth (%)	2.3	0.5	(0.2)	12.0	15.2
Emerging Markets	36,350	34,590	30,407	34,056	39,232
Growth (%)	(3.0)	(4.8)	(12.1)	12.0	15.2
Global API	5,290	6,260	6,930	7,415	8,160
Growth (%)	(28.3)	18.3	10.7	7.0	10.1
Total	146,300	152,200	158,913	178,869	204,106
Growth (%)	6.1	4.0	4.4	12.6	14.1

Source: HDFC sec Inst Research

Peer Set Comparison

	Mcap (Rs bn)	CMP (Rs/sh)	Reco	TP/FV	Adj EPS (Rs/sh)				P/E (x)				RoE (%)			
					FY18	FY19E	FY20E	FY21E	FY18	FY19E	FY20E	FY21E	FY18	FY19E	FY20E	FY21E
Sun Pharma	999	417	BUY	660	13.0	16.4	21.9	27.9	32.1	25.4	19.0	14.9	8.3	9.9	12.2	13.9
Dr Reddy's Labs	463	2,790	BUY	3,260	59.2	105.9	123.9	150.8	47.1	26.3	22.5	18.5	7.8	13.1	13.5	14.3
Aurobindo Pharma	445	760	NEU	845	41.4	40.6	55.7	56.4	18.4	18.7	13.7	13.5	23.0	18.6	21.1	17.8
Divi's Labs	439	1,653	SELL	1,395	32.4	51.0	56.8	65.7	51.1	32.4	29.1	25.2	15.2	21.1	20.3	20.4
Cipla	431	535	BUY	605	18.6	16.5	21.8	29.2	28.8	32.5	24.6	18.3	11.2	9.0	10.9	13.1
Lupin	381	842	BUY	985	38.0	13.5	32.5	48.5	22.1	62.4	25.9	17.4	12.7	4.4	10.0	13.7
Cadila Healthcare	325	318	BUY	480	13.0	15.9	19.3	22.8	24.4	19.9	16.5	14.0	17.0	17.2	17.7	17.9
Torrent Pharma	304	1,799	NEU	1,860	40.1	45.9	63.6	91.7	44.9	39.2	28.3	19.6	15.1	15.8	19.1	23.4
Alkem Laboratories	226	1,889	BUY	2,400	57.6	71.8	90.0	115.6	32.8	26.3	21.0	16.3	14.8	16.5	18.1	20.0
Glenmark	181	642	BUY	835	17.5	27.0	35.2	46.4	36.7	23.8	18.2	13.8	9.4	12.8	14.7	16.9
Jubilant Life Sciences	115	723	BUY	1,070	45.5	58.6	64.9	80.0	15.9	12.3	11.1	9.0	19.3	20.7	19.2	19.9
Alembic Pharma	109	580	NEU	580	21.9	24.1	24.7	34.7	26.5	24.0	23.5	16.7	20.0	18.6	16.2	19.7
Strides Shasun	37	417	BUY	585	12.7	5.5	30.8	39.3	32.8	76.2	13.5	10.6	4.4	1.9	9.7	11.4
Laurus Labs	37	346	BUY	480	15.8	8.4	17.7	29.8	21.9	41.0	19.5	11.6	11.9	4.6	11.5	16.9
Dishman Carbogen Amcis	31	194	BUY	380	13.2	16.0	20.9	26.7	14.7	12.1	9.3	7.3	14.6	15.2	16.7	18.1
Suven Life Sciences	28	219	NR	450	9.7	8.9	10.8	12.3	22.6	24.8	20.4	17.8	17.2	13.9	14.9	15.1
Granules India	22	86	BUY	160	5.2	9.3	11.3	14.2	16.4	9.2	7.6	6.0	12.0	16.9	17.8	19.1
Neuland Labs	6	481	BUY	885	11.0	15.5	51.8	67.2	43.9	31.0	9.3	7.2	2.2	3.2	9.1	10.8

Source: HDFC sec Inst Research

Change In Estimates (Consolidated)

Rs mn	Previous			New			% Chg		
	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E	FY19E	FY20E	FY21E
Revenue	161,969	184,066	209,971	159,647	182,369	208,106	(1.4)	(0.9)	(0.9)
EBITDA	28,183	34,409	42,112	27,140	33,751	42,053	(3.7)	(1.9)	(0.1)
APAT	14,058	18,023	23,552	13,254	17,530	23,507	(5.7)	(2.7)	(0.2)

Source: HDFC sec Inst Research

Income Statement (Consolidated)

Year ending March (Rs mn)	FY17	FY18	FY19E	FY20E	FY21E
Net Revenues	146,302	152,193	159,647	182,369	208,106
Growth (%)	6.1	4.0	4.9	14.2	14.1
Material Expenses	53,171	54,384	57,952	64,194	72,213
Employee Expenses	26,338	26,901	28,577	30,638	33,089
SG&A Expenses	7,608	7,610	7,663	8,936	9,989
Other Operating Expenses	34,427	35,034	38,315	44,850	50,762
EBITDA	24,758	28,264	27,140	33,751	42,053
EBITDA Margin (%)	16.9	18.6	17.0	18.5	20.2
EBITDA Growth (%)	-0.2	14.2	-4.0	24.4	24.6
Depreciation	13,229	13,228	11,054	11,861	12,794
EBIT	11,528	15,036	16,086	21,890	29,259
Other Income (Including EO Items)	2,287	2,801	4,500	3,500	4,050
Interest	1,594	1,142	1,691	1,550	1,499
PBT	12,221	16,695	18,895	23,840	31,810
Tax (Incl Deferred)	1,798	2,501	5,290	5,960	7,952
Minority Interest	(70)	(28)	(350)	(350)	(350)
RPAT	10,354	14,166	13,254	17,530	23,507
EO (Loss) / Profit (Net Of Tax)	-	(775)	-	-	-
APAT	10,354	14,941	13,254	17,530	23,507
APAT Growth (%)	-23.9	44.3	-11.3	32.3	34.1
Adjusted EPS (Rs)	12.9	18.6	16.5	21.8	29.2

Source: Company, HDFC sec Inst Research

Balance Sheet (Consolidated)

As at March (Rs mn)	FY17	FY18	FY19E	FY20E	FY21E
SOURCES OF FUNDS					
Share Capital - Equity	1,609	1,610	1,610	1,610	1,610
Reserves	123,645	140,682	151,583	166,760	187,915
Total Shareholders Funds	125,254	142,292	153,193	168,371	189,525
Minority Interest	4,382	3,524	3,524	3,524	3,524
Long Term Debt	36,454	36,621	31,621	28,621	25,621
Short Term Debt	4,672	4,359	4,359	4,359	4,359
Total Debt	41,126	40,980	35,980	32,980	29,980
Net Deferred Taxes	5,888	3,157	3,157	3,157	3,157
Long Term Provisions & Others	2,792	2,813	2,959	2,849	2,850
TOTAL SOURCES OF FUNDS	179,442	192,766	198,813	210,880	229,036
APPLICATION OF FUNDS					
Net Block	67,936	76,034	73,485	76,373	80,279
CWIP	16,877	5,124	5,065	5,560	5,562
Goodwill	26,784	28,147	28,147	28,147	28,147
Investments	141	107	107	107	107
Other Non-current Assets	7,510	7,707	6,142	5,332	4,521
Total Non-current Assets	119,248	117,118	112,945	115,519	118,615
Cash & Equivalents	15,848	22,148	38,789	42,596	50,580
Inventories	34,853	40,447	33,612	37,233	41,883
Debtors	24,974	31,025	28,258	32,279	36,835
Other Current Assets	12,927	15,991	17,590	19,349	21,284
Total Current Assets	72,754	87,463	79,460	88,861	100,003
Creditors	15,711	21,191	22,022	24,394	27,441
Other Current Liabilities & Provns	12,697	12,772	10,360	11,703	12,722
Total Current Liabilities	28,408	33,964	32,382	36,096	40,163
Net Current Assets	44,346	53,499	47,078	52,765	59,840
TOTAL APPLICATION OF FUNDS	179,442	192,766	198,813	210,880	229,036

Source: Company, HDFC sec Inst Research

Cash Flow (Consolidated)

Year ending March (Rs mn)	FY17	FY18	FY19E	FY20E	FY21E
Reported PBT	12,222	16,695	18,895	23,840	31,810
Non-operating & EO items	(1,079)	(1,385)	(2,475)	(2,475)	(2,479)
Interest expenses	1,594	1,142	1,691	1,550	1,499
Depreciation	13,229	13,228	11,054	11,861	12,794
Working Capital Change	2,354	(7,833)	8,132	(4,987)	(6,263)
Tax Paid	(4,503)	(7,220)	(5,290)	(5,960)	(7,952)
OPERATING CASH FLOW (a)	23,818	14,628	32,006	23,830	29,409
Capex	(10,982)	(7,395)	(8,447)	(15,245)	(16,702)
Free cash flow (FCF)	12,835	7,233	23,559	8,585	12,707
Investments	(2,307)	(509)	1,550	1,550	1,552
Non-operating Income	121	332	925	925	927
Others	66	(968)	-	-	-
INVESTING CASH FLOW (b)	(13,102)	(8,540)	(5,972)	(12,770)	(14,223)
Debt Issuance/(Repaid)	(10,803)	(345)	(5,000)	(3,000)	(3,000)
Interest Expenses	(1,594)	(1,178)	(1,691)	(1,550)	(1,499)
FCFE	(1,681)	4,565	19,343	6,510	10,687
Share Capital Issuance	120	1	(0)	--	0
Dividend	(1,936)	(1,893)	(2,353)	(2,353)	(2,353)
Others	1,158	741	(350)	(350)	(350)
FINANCING CASH FLOW (c)	(13,055)	(2,674)	(9,394)	(7,253)	(7,202)
NET CASH FLOW (a+b+c)	(2,339)	3,414	16,641	3,807	7,984
Equivalents (as at year end)	9,606	12,492	12,492	12,492	12,492
Closing Cash & Equivalents	15,848	22,148	38,789	42,596	50,580

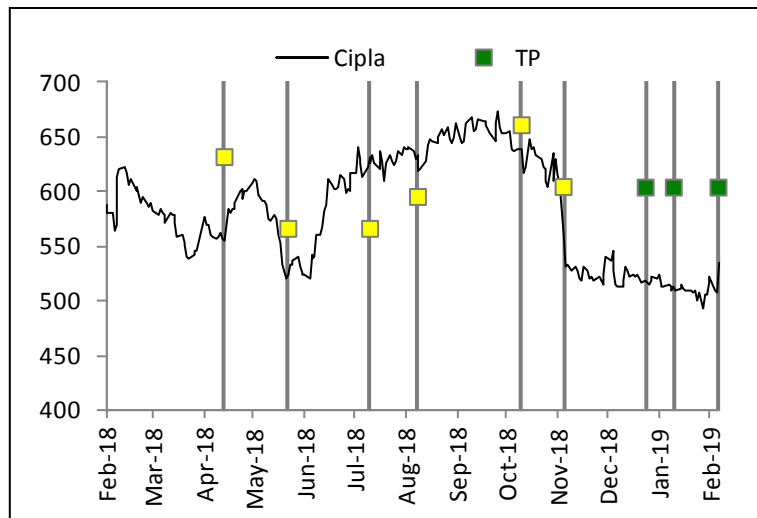
Source: Company, HDFC sec Inst Research

Key Ratios

	FY17	FY18	FY19E	FY20E	FY21E
PROFITABILITY (%)					
GPM	63.7	64.3	63.7	64.8	65.3
EBITDA Margin	16.9	18.6	17.0	18.5	20.2
APAT Margin	7.1	9.8	8.3	9.6	11.3
RoE	8.6	11.2	9.0	10.9	13.1
RoIC (or Core RoCE)	6.2	8.0	7.3	10.4	13.0
RoCE	6.5	8.6	7.4	9.1	11.2
EFFICIENCY					
Tax Rate (%)	14.7	15.0	28.0	25.0	25.0
Fixed Asset Turnover (x)	2.4	2.0	2.0	2.0	2.1
Inventory (days)	87.0	97.0	76.8	74.5	73.5
Debtors (days)	62.3	74.4	64.6	64.6	64.6
Other Current Assets (days)	32.3	38.4	40.2	38.7	37.3
Payables (days)	39.2	50.8	50.3	48.8	48.1
Other Current Liab & Provns (days)	31.7	30.6	23.7	23.4	22.3
Cash Conversion Cycle (days)	110.6	128.3	107.6	105.6	105.0
Debt/EBITDA (x)	1.7	1.4	1.3	1.0	0.7
Net D/E (x)	0.2	0.1	(0.0)	(0.1)	(0.1)
Interest Coverage (x)	7.2	13.2	9.5	14.1	19.5
PER SHARE DATA (Rs)					
EPS	12.9	18.6	16.5	21.8	29.2
CEPS					
Dividend	2.0	2.5	2.5	2.5	2.5
Book Value	155.7	176.9	190.4	209.3	235.6
VALUATION					
P/E (x)	41.6	28.8	32.5	24.6	18.3
P/BV (x)	3.4	3.0	2.8	2.6	2.3
EV/EBITDA (x)	18.4	15.9	15.8	12.5	9.7
EV/Revenues (x)	3.1	3.0	2.7	2.3	2.0
OCF/EV (%)	5.2	3.3	7.5	5.7	7.2
FCF/EV (%)	2.8	1.6	5.5	2.0	3.1
FCFE/Mkt Cap (%)	(0.4)	1.1	4.5	1.5	2.5
Dividend Yield (%)	0.4	0.5	0.5	0.5	0.5

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
13-Apr-18	556	NEU	631
23-May-18	524	NEU	565
10-Jul-18	623	NEU	565
9-Aug-18	633	NEU	595
10-Oct-18	639	NEU	660
6-Nov-18	564	NEU	605
26-Dec-18	519	BUY	605
10-Jan-19	514	BUY	605
7-Feb-19	535	BUY	605

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

INSTITUTIONAL RESEARCH

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