

Sector: Pharmaceuticals
Result Update

	Change
Reco: Hold	↔
CMP: Rs. 234	
Price Target: Rs. 275	↓

↑ Upgrade ↔ No change ↓ Downgrade

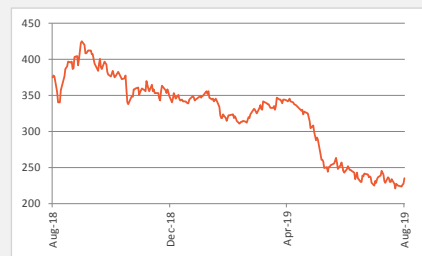
Company details

Market cap:	Rs. 23,962 cr
52-week high/low:	Rs. 432 / 216
NSE volume: (No of shares)	20.2 lakh
BSE code:	532321
NSE code:	CADILAHC
Sharekhan code:	CADILAHC
Free float: (No of shares)	25.8 cr

Shareholding (%)

Promoters	74.8
FII	5.0
DII	11.6
Others	8.64

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	6.1	-16.9	-26.0	-36.6
Relative to Sensex	9.7	-16.4	-28.2	-36.5

Sharekhan Research, Bloomberg

Cadila Healthcare Limited (Cadila) reported 22.2% y-o-y growth in total operating revenue to Rs. 3,496.3 crore (2% above estimate). Operating profit (adjusted for one-time cost of Rs. 70 related to acquisition) reported 14.8% y-o-y growth to Rs. 702 crore (6.5% above estimate); OPM declined by 130 BPS y-o-y to 20.1% (100 BPS above our estimate of 19.1%). Adjusted profit grew by 14.5% to Rs. 384.8 crore (11.9 % above estimates). Strong sales growth was mainly due to consumer wellness business in India (acquisition led). India human formulation reported 6% y-o-y growth, U.S. business reported 11.2% y-o-y growth and EM and LATAM business reported 12.3% y-o-y growth. USFDA has recently classified Cadila's Moraiya facility as Official Action Indicated (OAI). Although this development does not affect the current operations of the U.S. business, it is likely to delay pending approvals from this site (32-35 pending ANDAs).

Key positives

- Operating margin of 20.1% (adjusted for one-off costs) is better than expectation.
- The company plans to transfer pending approval ANDAs (injectables) from Moraiya facility to Liva facility to de-risk delay in approvals.
- Management expects the U.S. and India businesses to grow in double digits and high single digit, respectively, for FY2020 despite competition in the U.S. business and restructuring of India formulation business.
- Biologics and vaccines business to propel growth and profitability from FY2021E.

Key negatives

- Gross margin for the quarter declined by 153 BPS to 64%.
- Escalation of Moraiya facility to OAI by the USFDA.

Our Call

Valuation - Maintain Hold with marginally downward revised PT of Rs. 275: The stock has corrected by ~45% from its high and is currently trading at 11.4x its FY2021E earnings. We expect the company to report sales and profit CAGR of 11% and 8%, respectively, over the next two years. Although the quarter's performance was better than expectation, recent classification of Moraiya facility to OAI by the USFDA has dampened sentiments. This development does not impact ongoing operations but could delay new product approvals and remediation and re-inspection of the facility could take 6-9 months. Thus, we feel although the valuation is reasonable, if Moraiya issues get escalated to an import alert, earnings can be downgraded. We would like to wait until further clarity emerges. Hence, we maintain our Hold rating on the stock with marginally downward revised PT of Rs. 275.

Key Risks

- Regulatory compliance remains key risk; 2) Exchange rate/Forex volatility could impact earnings.

Valuation (Consolidated)

Particulars	FY2018	FY2019	FY2020E	FY2021E
Net sales	11,954.5	13,165.6	14,372.5	16,175.2
OPM (%)	23.8	22.6	22.1	22.2
Adjusted Net profit	1,731.9	1,801.9	1,853.3	2,097.9
EPS (Rs.)	16.9	17.6	18.1	20.5
PER (x)	13.8	13.3	12.9	11.4
EV/EBITDA (x)	10.2	10.9	9.7	8.3
P/BV (x)	2.7	2.3	2.0	1.8
D:E	0.74	0.87	0.66	0.58
RoCE (%)	15.4	12.3	12.6	13.2
RoNW(%)	19.8	17.3	15.8	15.7

Source: Company, Sharekhan Estimates

Overall business to remain stable: U.S. business outlook remains stable and management plans ~25 launches in the U.S. for FY2020 (excluding approvals and launches from Moraiya facility as it has been classified as OAI in August 2019). Management plans site transfer of ~32 pending products from Moraiya to Liva facility to de-risk the delay in approvals. Moreover, India business is likely to report high single-digit growth in FY2020 despite new product launches and rationalisation of product portfolio. Biosimilars, specialty products and vaccines are other growth drivers that will propel growth from FY2021. Hence, overall, we expect the company to deliver sales and profit CAGR of modest 11% and 8%, respectively, over FY2019-FY2021. Moreover, margins are expected to remain under pressure as the company witnesses competitive pressure in its niche launches and remediation costs will also weigh in the near term.

Results

					Rs cr
Particulars	Q1FY2020	Q1FY2019	YoY %	Q4FY2019	QoQ%
Total Operating revenue	3,496.3	2,860.3	22.2	3,732.8	-6.3
Expenditure	2,794.3	2,248.7	24.3	2,932.4	-4.7
Operating profit	702.0	611.6	14.8	800.4	-12.3
Other Income	22.6	21.7	4.1	38.4	-41.1
EBITDA	724.6	633.3	14.4	838.8	-13.6
Interest	89.1	35.0	154.6	77.3	15.3
Depreciation	171.6	141.8	21.0	155.6	10.3
PBT	463.9	456.5	1.6	605.9	-23.4
Taxes	79.1	120.3	-34.2	126.7	-37.6
Adjusted PAT	384.8	336.2	14.5	479.2	-97.0
Extra-Ordinary item + MI	-81.2	131.0		-19.1	
Reported PAT	303.6	467.2	-35.0	460.1	-34.0
Reported EPS (Rs.)	3.0	4.6	-35.0	4.5	-34.0
Margins			BPS		BPS
OPM %	20.1	21.4	-130.4	21.4	-136.4
PATM %	8.7	16.3	-765.0	12.3	-364.2
Tax rate %	17.1	26.4	-930.2	20.9	-386.0

Source: Company; Sharekhan Research

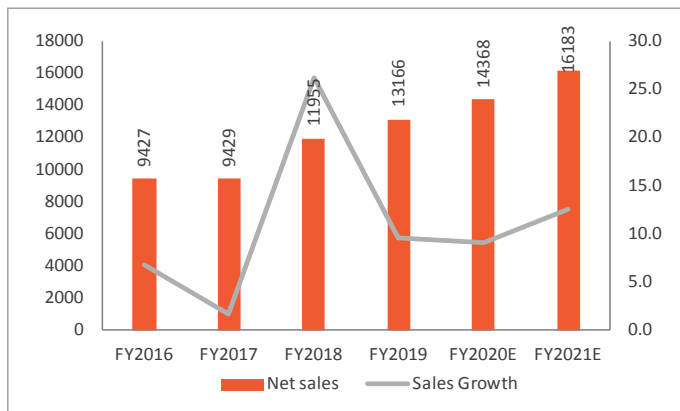
Geographical Sales Break-Up – Quarterly

					Rs cr
Revenue break-up	Q1FY2020	Q1FY2019	YoY %	Q4FY2019	QoQ %
India	1674.5	1146.3	46.1%	1429.7	17.1%
Human formulations	947.6	892.6	6.2%	902.3	5.0%
Consumer Wellness	606.4	128.8	370.8%	402.1	50.8%
Animal Health & Others	120.5	124.9	-3.5%	125.3	-3.8%
U.S. Formulation	1367.0	1229.6	11.2%	1795.4	-23.9%
EM & LATAM Formulations	220.4	196.3	12.3%	207.2	6.4%
Europe Formulations	47.4	61.8	-23.3%	53.5	-11.4%
APIs	69.2	109.5	-36.8%	96.0	-27.9%
Alliances	27.8	25.3	9.9%	37.7	-26.3%
Grand Total	3406.3	2768.8	23.0%	3619.5	-5.9%
OOI	90.1	91.6	-1.6%	113.3	-20.5%
Total Operating Revenue	3496.4	2860.4	22.2%	3732.8	-6.3%

Source: Company, Sharekhan Research, Industry Reports

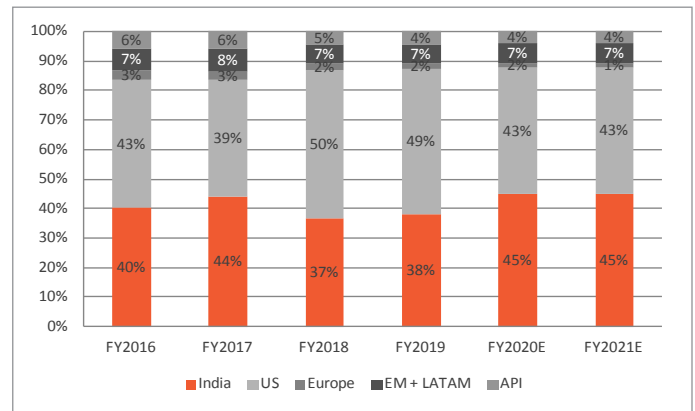
Financials in charts

Sales and Sales Growth



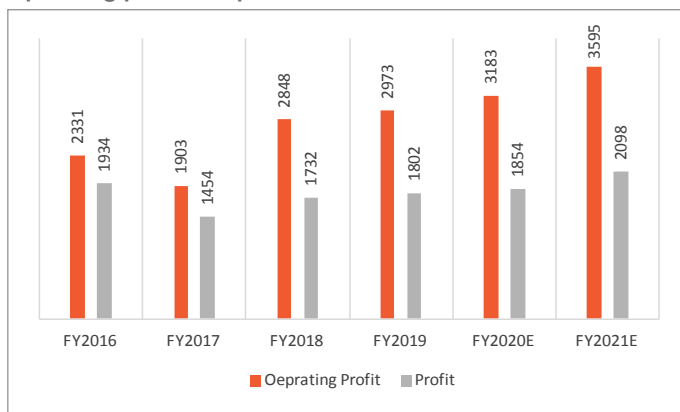
Source: Company, Sharekhan Research

Geography-wise sales break-up



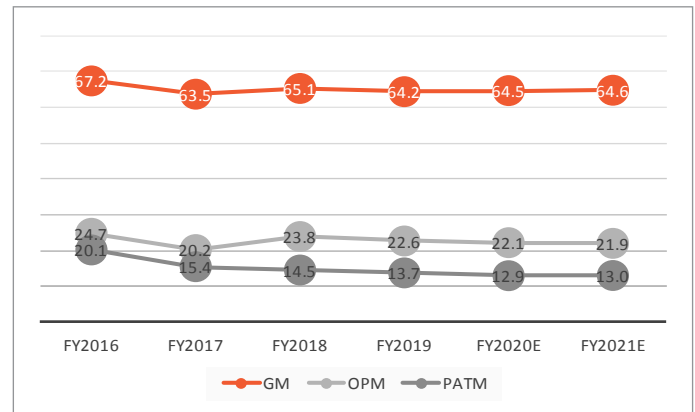
Source: Company, Sharekhan Research

Operating profit and profit



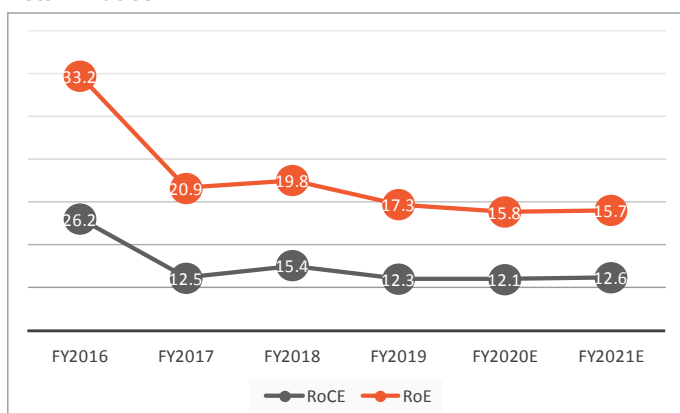
Source: Company, Sharekhan Research

Margin profile



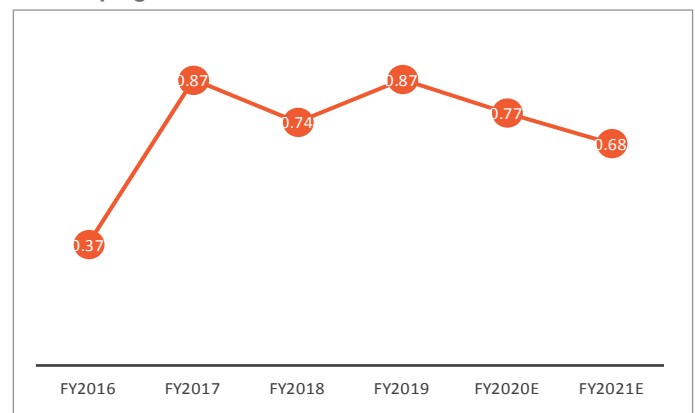
Source: Company, Sharekhan Research

Return Ratios



Source: Company, Sharekhan Research

Debt: Equity Ratio



Source: Company, Sharekhan Research

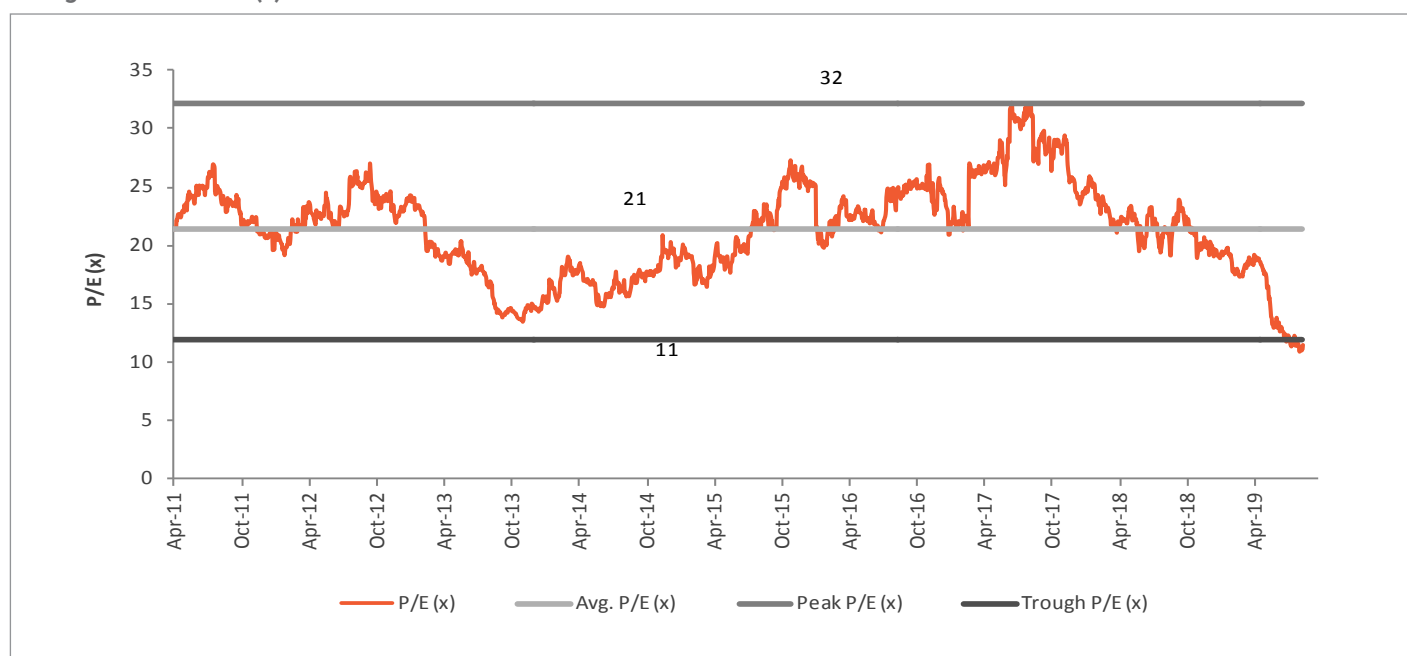
Outlook

Cadila is favourably progressing in its efforts to build an alternative growth platform (NCE, Biologics and Vaccines) that should start delivering from FY2021 and reduce the company's dependence on limited competition assets in the U.S. for its earnings. Moreover, OPM improvement and, in turn, profitability would be visible from FY2021E.

Valuation - Maintain Hold with marginally downward revised PT of Rs. 275

The stock has corrected by ~45% from its high and is currently trading at 11.4x its FY2021E earnings. We expect the company to report sales and profit CAGR of 11% and 8%, respectively, over the next two years. However, recent classification of Moraiya facility to OAI by the USFDA has dampened sentiments. This development does not impact ongoing operations but could delay new product approvals and remediation and re-inspection of the facility could take 6-9 months. Thus, we feel although the valuation is reasonable, if Moraiya issues get escalated to an import alert, earnings can be downgraded. We would like to wait until further clarity emerges. Hence, we maintain our Hold rating on the stock with marginally downward revised PT of Rs. 275.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer Comparison

Particulars	P/E (x)		EV/EBIDTA (x)		RoE (%)		D: E	
	FY20E	FY21E	FY20E	FY2021E	FY20E	FY21E	FY20E	FY21E
Aurobindo	10.9	9.3	6.7	5.8	20.7	19.8	0.50	0.40
Cadila	12.9	11.4	9.4	8.2	15.8	15.8	0.80	0.70
Cipla	18.8	13.4	11.9	8.7	12.8	15.4	0.25	0.18
Lupin	27.0	21.6	10.4	8.4	7.2	8.2	0.54	0.48
Sun Pharma	18.7	13.7	11.5	8.0	11.7	13.9	0.24	0.21
Torrent Pharma	28.0	17.5	11.3	7.9	11.7	13.9	0.21	0.17

Source: Sharekhan Research

About company

Cadila is one of the leading pharmaceutical companies in India with presence across the pharmaceutical value chain of research, development, manufacturing, marketing and selling of finished dosage human formulations (generics, branded generics and specialty formulations, including biosimilars and vaccines), active pharmaceutical ingredients (APIs), animal healthcare products and consumer wellness products. The company has a global presence and sells its products in the U.S., India, Europe and emerging markets, including countries in Latin America, Asia Pacific region and Africa. The company is also engaged in research and development activities focused across the value chain of API process development, generics development for simple as well as differentiated dosage forms such as modified release oral solids, transdermals, topicals and nasals, biologics, vaccines, and new chemical entities (NCE).

Investment theme

The USFDA regulatory hurdle at one of the key manufacturing facilities, Moraiya (recently classified as OAI) is likely to delay new approvals from this unit. Although the company is reducing its dependence on this unit, this news continues to remain an overhang. Cadila still expects 20-30 new approvals from other plants, of which 10 should be limited competition. Most of its transdermal filings will also not be impacted. The company is favourably progressing in its efforts to build an alternative growth platform (NCE, Biologics and Vaccines), which should start delivering from FY2021 and reduce Cadila's dependence on limited competition assets in the U.S. for its earnings. Zydus wellness and the domestic portfolio should grow in high single digits to mid-teens and should lead to margin expansion.

Key Risks

1) Regulatory compliance risk; 2) delay in product approvals; 3) currency risk; and 4) concentration risk in the U.S. portfolio

Additional Data

Key management personnel

Pankaj R. Patel	Chairman
Dr. Sharvil P. Patel	Managing Director
Mr. Ganesh Nayak	COO & Executive Director
Mr. Nitin Parekh	CFO

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Zydus Family Trust	74.8
2	Life Insurance Corp of India	2.8
3	Kotak Mahindra Asset Management Co	1.9
4	Franklin Resources Inc	1.6
5	Government Pension Fund - Global	1.1
6	Norges Bank	1.1
7	UTI Asset Management Co Ltd	1.0
8	Vanguard Group Inc	0.9
9	FundRock Management Co SA	0.7
10	Reliance Capital Trustee Co Ltd	0.7

Source: Bloomberg

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