

BUY

TP: Rs 570 | ▲ 27%

CIPLA

Pharmaceuticals

05 February 2020

EBITDA a tad lower but India/US deliver a good beat; retain BUY

Cipla's adj. EBITDA missed estimates by 3% due to lower gross margins which saw a 120bps one-off impact. While EM sales were weak (deferred shipments), key positives in India (+12% YoY) and the US drove in-line revenues at Rs 43.7bn. Adj. EBITDA margin was 18.5%, 60bps lower than expected. India ROI leverage (by integrating Rx, generics, consumer health) and lower R&D spends in FY21 should enable Cipla to meet our FY21/FY22 EPS estimates. gAlbuterol deferral to H2FY21 (from H1) is negative. Retain BUY with a TP of Rs 570.

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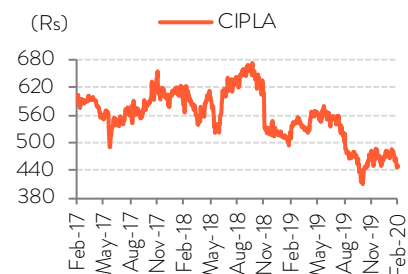
India, US beat continues: India sales growth beat estimates at 12% YoY (branded sales grew 14% YoY, trade generics 7%). Cipla has talked of an integrated approach and leveraging the distribution channel for India business, which should boost prescription (Rx) volume growth and maximise returns. US sales were a 4% beat at US\$ 133mn and management expects a US\$ 120mn-130mn base to be maintained. R&D spends should moderate in FY21 given that Advair generic trials are over (readouts by Mar'20; US\$ 25mn spent on Advair in 9MFY20). Cipla clarified that incremental specialty spends will not be at the cost of margins.

Ticker/Price	CIPLA IN/Rs 448
Market cap	US\$ 5.1bn
Shares o/s	806mn
3M ADV	US\$ 18.7mn
52wk high/low	Rs 586/Rs 390
Promoter/FPI/DII	37%/26%/13%

Source: NSE

Earnings takeaways: (1) US specialty R&D spends in FY21 to be 1% of overall sales with a key focus on the hospital segment; top 3 products in the US form 25% of sales. (2) Gross margin impact due to shelf stock adjustments on gSensipar and overhead charges as per accounting standards. (3) Shipment to EMs deferred to Q4. (4) Coronavirus escalation in Mar'20 would affect the entire industry.

STOCK PERFORMANCE



Source: NSE

Implied valuation for US business attractive: We continue to expect a core EPS CAGR of 15-18% over FY19-FY22. About 70% of FY22E EBITDA is from branded generics (India, S. Africa, ROW). At CMP, US implied value is attractive at 2x FY21E EV/EBITDA (7x for peers). Advair presents an upside risk to our EPS estimates.

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	152,181	163,604	169,751	179,280	192,699
EBITDA (Rs mn)	28,254	30,955	33,166	34,944	38,654
Adj. net profit (Rs mn)	12,340	13,409	16,057	17,667	20,160
Adj. EPS (Rs)	15.3	16.6	19.9	21.9	25.0
Adj. EPS growth (%)	(0.2)	8.7	19.7	10.0	14.1
Adj. ROAE (%)	8.9	9.0	10.1	10.2	10.6
Adj. P/E (x)	29.2	26.9	22.5	20.4	17.9
EV/EBITDA (x)	13.9	12.4	11.4	10.5	9.0

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)	Q3FY20E	Var (%)	9MFY20	9MFY19	YoY (%)
Net Sales	43,709	40,075	9.1	43,957	(0.6)	43,835	(0.3)	127,555	119,583	6.7
EBITDA	8,084	7,078	14.2	9,096	(11.1)	8,360	(3.3)	26,227	21,369	22.7
Depreciation	2,778	2,931	-	2,829	-	2,829	-	8,287	8,160	-
EBIT	5,306	4,147	27.9	6,267	(15.3)	5,531	-	17,940	13,209	-
Interest	461	442	-	460	-	400	-	1,442	1,235	-
Other Income	721	785	-	1,005	-	500	-	2,509	2,960	-
PBT	5,566	4,490	24.0	6,812	(18.3)	5,631	(1.2)	19,007	14,934	27.3
Less: Taxation	1,528	1,256	-	2,005	-	1,577	-	5,455	4,416	-
Less: Minority Interest	26	(99)	-	90	-	0	-	41	(254)	-
Recurring PAT	4,012	3,333	20.4	4,717	(14.9)	4,055	(1.1)	13,511	10,772	25.4
Exceptional Items	0	0	-	0	-	0	-	0	850	-
Reported PAT	4,012	3,333	20.4	4,717	(14.9)	4,055	(1.1)	13,511	11,622	16.3
Key Ratios (%)										
Gross Margin	63.5	63.5	-	66.8	-	65.5	-	66.7	64.1	-
EBITDA Margin	18.5	17.7	-	20.7	-	19.1	-	20.6	17.9	-
Tax / PBT	27.5	28.0	-	29.4	-	28.0	-	28.7	29.6	-
NPM	9.2	8.3	-	10.7	-	9.2	-	10.6	9.0	-
EPS (Rs)	5.0	4.1	-	5.9	-	5.0	-	16.8	13.4	-

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)	Q3FY20E	Var (%)	9MFY20	9MFY19	YoY (%)
Formulations	40,670	37,910	7.3	40,790	(0.3)	41,441	(1.9)	117,910	112,100	5.2
India	17,770	15,850	12.1	17,450	1.8	17,119	3.8	48,770	47,730	2.2
US	9,460	8,490	11.4	9,530	(0.7)	9,088	4.1	30,180	22,765	32.6
SAGA	8,310	7,750	7.2	7,400	12.3	8,333	(0.3)	22,620	23,630	(4.3)
South Africa	5,940	5,570	6.6	5,460	8.8	5,733	3.6	16,720	16,380	2.1
Others/Global Access	2,370	2,180	8.7	1,940	22.2	2,600	(8.8)	5,900	7,250	(18.6)
Europe	1,900	1,890	0.5	1,900	0.0	2,041	(6.9)	5,810	4,640	25.2
ROW	3,230	3,930	(17.8)	4,510	(28.4)	4,860	(33.5)	10,530	13,335	(21.0)
APIs	1,650	1,540	7.1	1,570	5.1	1,694	(2.6)	5,040	5,250	(4.0)
Other Op. income	1,400	640	118.8	1,590	(11.9)	700	100.0	4,590	2,189	109.7
Net Sales	43,720	40,090	9.1	43,950	(0.5)	43,835	(0.3)	127,540	119,539	6.7

Source: Company, BOBCAPS Research

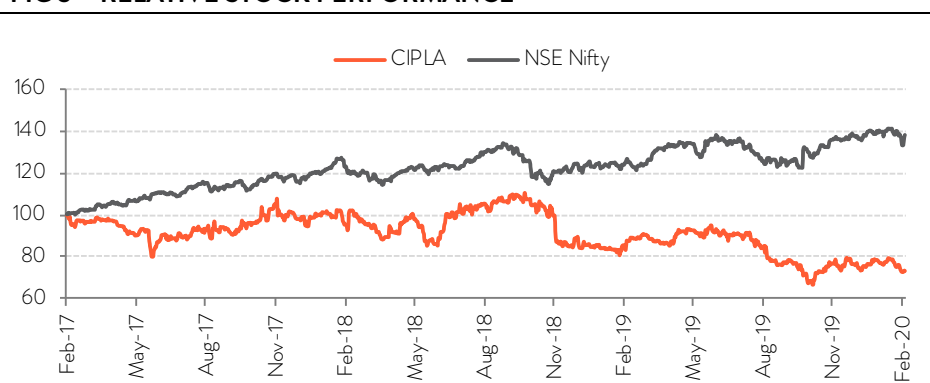
Valuation methodology

We like Cipla for its strong India franchise, rich US pipeline and low risk of price erosion in the US market (top 3 products form 25% of US sales). Operating leverage in the US business will be a key margin driver in the next two years. We believe Cipla’s future investments will have a sharper focus on opportunities in high-value/complex assets, but not at the cost of current margins.

We retain our FY20-FY22 EPS estimates and Mar’21 target price to Rs 570, based on 12x EV/EBITDA (24x implied P/E). We believe the Goa plant OAI (official action indicated) risk is largely priced in given that existing sales based on a single sourced product would be US\$ 50mn-60mn or 2.5% of FY19 sales (6% on total product basis). Also, none of the pending files from this site are due for approval in the next 15 months. Hence, any material impact on earnings trajectory appears unlikely.

We continue to expect a core EPS CAGR of 15-18% over FY19-FY22. Advair approval represents an upside risk to our EPS estimates. We have valued one-time gSensipar at non-core business multiples. Maintain BUY.

FIG 3 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **US execution critical:** We expect the US market to contribute meaningfully to profitability in the coming years. Any delay in key launches (Proventil HFA, Flonase) can potentially erode 4-5% of FY21E EPS.
- **Reduction in Global Access funding:** A decline in the tender-facing Global Access business due to challenges in the funding environment poses a risk to our estimates.
- **Weak drug price hikes in South Africa**

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue	152,181	163,604	169,751	179,280	192,699
EBITDA	28,254	30,955	33,166	34,944	38,654
Depreciation	13,228	13,263	12,080	13,046	14,090
EBIT	15,026	17,692	21,086	21,897	24,564
Net interest income/(expenses)	(1,142)	(1,684)	(1,480)	(1,002)	(626)
Other income/(expenses)	984	2,915	3,331	3,643	4,063
Exceptional items	0	0	0	0	0
EBT	14,868	18,924	22,938	24,538	28,001
Income taxes	2,501	5,696	6,881	6,871	7,840
Extraordinary items	1,817	1,850	0	0	0
Min. int./Inc. from associates	27	(181)	0	0	0
Reported net profit	14,157	15,259	16,057	17,667	20,160
Adjustments	1,817	1,850	0	0	0
Adjusted net profit	12,340	13,409	16,057	17,667	20,160

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	21,191	19,480	22,681	23,980	25,803
Other current liabilities	7,904	10,126	9,934	10,503	11,302
Provisions	7,650	8,582	8,897	9,407	10,122
Debt funds	40,980	43,161	30,829	19,268	12,043
Other liabilities	0	0	0	0	0
Equity capital	1,610	1,611	1,611	1,611	1,611
Reserves & surplus	147,378	154,016	167,655	182,906	200,649
Shareholders' fund	148,988	155,627	169,267	184,517	202,261
Total liabilities and equities	226,713	236,976	241,608	247,675	261,531
Cash and cash eq.	9,655	6,188	14,937	19,606	28,148
Accounts receivables	31,020	41,507	34,928	35,010	37,673
Inventories	40,450	39,648	43,093	45,561	49,026
Other current assets	23,697	21,866	23,180	24,507	26,371
Investments	12,586	25,539	25,539	25,539	25,539
Net fixed assets	53,154	51,144	49,996	48,756	47,417
CWIP	9,813	6,762	6,762	6,762	6,762
Intangible assets	46,337	44,322	43,174	41,934	40,595
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	226,712	236,975	241,608	247,675	261,531

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	27,385	28,522	28,136	30,714	34,250
Interest expenses	1,142	1,684	1,480	1,002	626
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(9,765)	(6,412)	5,145	(1,500)	(4,653)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	18,761	23,794	34,762	30,215	30,224
Capital expenditures	(17,369)	(6,228)	(10,932)	(11,807)	(12,751)
Change in investments	(2,856)	(12,953)	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(20,225)	(19,181)	(10,932)	(11,807)	(12,751)
Equities issued/Others	1	1	0	0	0
Debt raised/repaid	(146)	2,181	(12,332)	(11,561)	(7,226)
Interest expenses	(1,142)	(1,684)	(1,480)	(1,002)	(626)
Dividends paid	(1,609)	(2,417)	(2,417)	(2,417)	(2,417)
Other financing cash flows	7,775	(6,163)	1,148	1,240	1,339
Cash flow from financing	4,879	(8,082)	(15,081)	(13,740)	(8,930)
Changes in cash and cash eq.	3,415	(3,468)	8,749	4,668	8,542
Closing cash and cash eq.	9,656	6,187	14,937	19,606	28,148

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	17.6	18.9	19.9	21.9	25.0
Adjusted EPS	15.3	16.6	19.9	21.9	25.0
Dividend per share	3.0	3.0	3.0	3.0	3.0
Book value per share	180.8	189.3	206.6	225.5	247.6

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	2.6	2.3	2.2	2.0	1.8
EV/EBITDA	13.9	12.4	11.4	10.5	9.0
Adjusted P/E	29.2	26.9	22.5	20.4	17.9
P/BV	2.5	2.4	2.2	2.0	1.8

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	83.0	70.9	70.0	72.0	72.0
Interest burden (PBT/EBIT)	98.9	107.0	108.8	112.1	114.0
EBIT margin (EBIT/Revenue)	9.9	10.8	12.4	12.2	12.7
Asset turnover (Revenue/Avg TA)	20.8	21.0	21.3	22.2	23.0
Leverage (Avg TA/Avg Equity)	1.3	1.3	1.3	1.2	1.1
Adjusted ROAE	8.9	9.0	10.1	10.2	10.6

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
YoY growth (%)					
Revenue	4.1	7.5	3.8	5.6	7.5
EBITDA	14.9	9.6	7.1	5.4	10.6
Adjusted EPS	(0.2)	8.7	19.7	10.0	14.1
Profitability & Return ratios (%)					
EBITDA margin	18.6	18.9	19.5	19.5	20.1
EBIT margin	9.9	10.8	12.4	12.2	12.7
Adjusted profit margin	8.1	8.2	9.5	9.9	10.5
Adjusted ROAE	8.9	9.0	10.1	10.2	10.6
ROCE	8.7	10.6	12.2	12.6	13.7
Working capital days (days)					
Receivables	77	95	77	73	73
Inventory	100	91	95	95	95
Payables	52	45	50	50	50
Ratios (x)					
Gross asset turnover	1.2	1.2	1.2	1.1	1.1
Current ratio	2.9	2.9	2.8	2.8	3.0
Net interest coverage ratio	13.2	10.5	14.2	21.9	39.2
Adjusted debt/equity	0.1	0.1	0.0	(0.1)	(0.2)

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

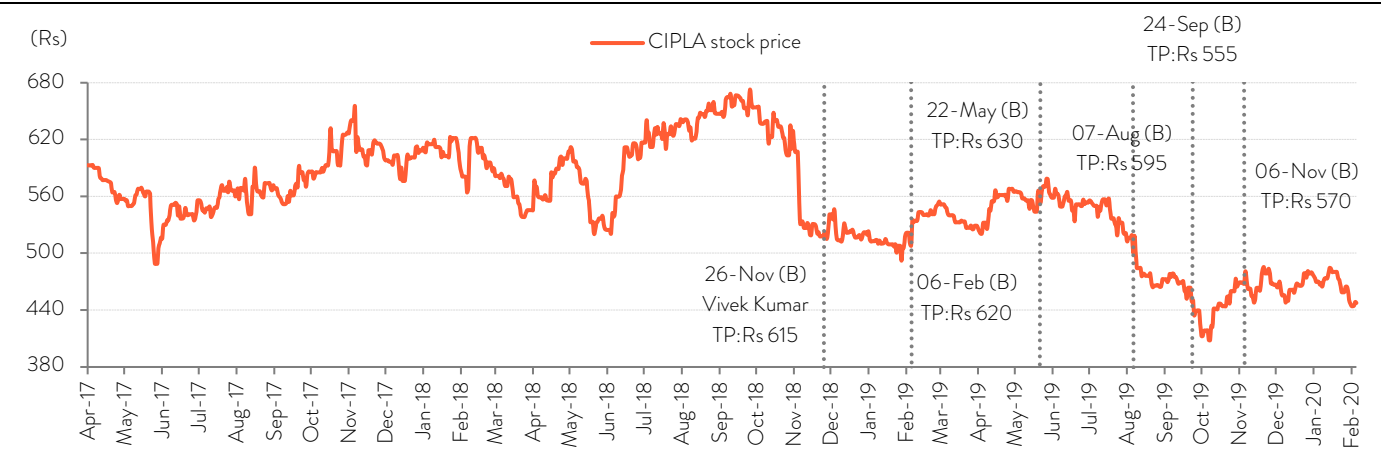
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

HISTORICAL RATINGS AND TARGET PRICE: CIPLA (CIPLA IN)



B – Buy, A – Add, R – Reduce, S – Sell

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