

BUY

TP: Rs 690 | ▲ 21%

CIPLA

Pharmaceuticals

16 May 2020

Adj. EBITDA in line; multiple stock catalysts – BUY

Cipla reported in-line revenue but a 14% EBITDA miss in Q4. Adjusting for one-offs – Covid-19 impact on gross margin (200bps) and Goa unit remediation cost (1% of sales) – EBITDA broadly met estimates at Rs 7.3bn. India sales were a beat; the US was in line. Managing the supply chain, optimising costs and improving ROI are focus areas for FY21. Albuterol ramp-up, Advair filings and a strong branded franchise are key stock catalysts. We raise our TP to Rs 690 (vs. Rs 570) as Cipla's resilient model merits a higher 14x EV/EBITDA multiple (vs. 12x).

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India continues to outperform, US in line; utilisation back to pre-Covid levels:

Cipla's strategy of fusing brands (CH+Rx+Gx) led to strong India growth at 15% YoY in Q4 (branded +12% YoY, trade generics +15%). Growth could have been higher but for Covid-19 which hit ~Rs 2bn worth of high-margin India sales. Demand within India is intact and stockist channels have a fair amount of inventory. US sales at US\$ 118mn fell 11% QoQ due to higher chargebacks; base sales are likely to remain in the US\$ 120mn-130mn range. Cipla continues to expect calibrated R&D spends in the generic and US specialty segments. Roughly, 85% capacity utilisation is back to pre-Covid-19 levels across locations.

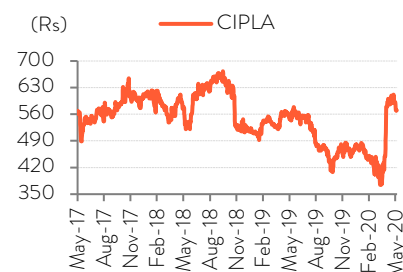
Earnings call takeaways: (1) Albuterol market grew 15% amidst Covid (~65mn units) and pricing is fairly attractive. Proair/Proventil markets are interchangeable; production capacities suffice to garner adequate market share with staggered launch. (2) Reply on Goa unit (warning letter) submitted in Apr'20. (3) Repaid US\$ 275mn debt in FY20; Q4 depreciation has Rs 323mn impairment charge.

Retain BUY: Earnings stability with ~70% of EBITDA arising from branded generics (India, S. Africa, ROW), US generic tailwinds amidst Covid-19 (price + drug shortages), and product catalysts (Albuterol, Advair) are stock drivers. We raise our Mar'21 TP to Rs 690 (vs. Rs 570), set at 14x EV/EBITDA (12x earlier).

Ticker/Price	CIPLA IN/Rs 570
Market cap	US\$ 6.1bn
Shares o/s	806mn
3M ADV	US\$ 55.8mn
52wk high/low	Rs 633/Rs 355
Promoter/FPI/DII	37%/26%/13%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
Total revenue (Rs mn)	152,181	163,621	171,243	178,060	191,896
EBITDA (Rs mn)	28,254	30,973	32,574	34,388	38,265
Adj. net profit (Rs mn)	12,340	13,426	15,858	17,424	19,896
Adj. EPS (Rs)	15.3	16.7	19.7	21.6	24.7
Adj. EPS growth (%)	(0.2)	8.8	18.1	9.9	14.2
Adj. ROAE (%)	8.9	9.0	10.0	10.1	10.5
Adj. P/E (x)	37.2	34.2	29.0	26.4	23.1
EV/EBITDA (x)	17.4	15.6	14.7	13.6	11.7

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	Q4FY20E	Var (%)	FY20P	FY19	YoY (%)
Net Sales	43,761	44,039	(0.6)	43,709	0.1	43,159	1.4	171,316	163,622	4.7
EBITDA	6,336	9,611	(34.1)	8,084	(21.6)	7,385	(14.2)	32,563	30,980	5.1
Depreciation	3,459	5,100	-	2,778	-	2,778	-	11,746	13,260	-
EBIT	2,877	4,511	(36.2)	5,306	(45.8)	4,607	-	20,817	17,720	-
Interest	530	447	-	461	-	400	-	1,972	1,682	-
Other Income	931	953	-	721	-	500	-	3,440	3,913	-
PBT	3,278	5,017	(34.7)	5,566	(41.1)	4,707	(30.4)	22,285	19,951	11.7
Less: Taxation	855	1,277	-	1,528	-	1,318	-	6,310	5,693	-
Less: Minority Interest	(36)	64	-	26	-	0	-	5	(190)	-
Recurring PAT	2,459	3,676	(33.1)	4,012	(38.7)	3,389	(27.4)	15,970	14,448	10.5
Exceptional Items	0	0	-	0	-	0	-	0	850	-
Reported PAT	2,459	3,676	(33.1)	4,012	(38.7)	3,389	(27.4)	15,970	15,298	4.4
Key Ratios (%)										
Gross Margin	61.4	66.3	-	63.5	-	64.5	-	65.3	64.6	-
EBITDA Margin	14.5	21.8	-	18.5	-	17.1	-	19.0	18.9	-
Tax / PBT	26.1	25.5	-	27.5	-	28.0	-	28.3	28.5	-
NPM	5.6	8.3	-	9.2	-	7.9	-	9.3	8.8	-
EPS (Rs)	3.1	4.6	-	5.0	-	4.2	-	19.9	18.0	-

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	Q4FY20E	Var (%)	FY20P	FY19	YoY (%)
Formulations	40,580	41,080	(1.2)	40,670	(0.2)	40,245	0.8	158,490	153,180	3.5
India	17,300	15,000	15.3	17,770	(2.6)	16,500	4.8	66,070	62,730	5.3
US	8,560	11,430	(25.1)	9,460	(9.5)	8,856	(3.3)	38,740	34,195	13.3
SAGA	8,250	8,230	0.2	8,310	(0.7)	8,310	(0.7)	30,870	31,860	(3.1)
South Africa	5,320	5,130	3.7	5,940	(10.4)	5,940	(10.4)	22,040	21,510	2.5
Others/Global Access	2,930	3,100	(5.5)	2,370	23.6	2,370	23.6	8,830	10,350	(14.7)
Europe	2,320	2,360	(1.7)	1,900	22.1	2,549	(9.0)	8,130	7,000	16.1
ROW	4,150	4,060	2.2	3,230	28.5	4,030	3.0	14,680	17,395	(15.6)
APIs	2,470	1,740	42.0	1,650	49.7	1,914	29.0	7,510	6,990	7.4
Other Op. income	711	1,219	(41.7)	1,400	(49.2)	1,000	(28.9)	5,301	3,408	55.5
Net Sales	43,761	44,039	(0.6)	43,720	0.1	43,159	1.4	171,301	163,578	4.7

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 expense of current margins.

We retain BUY and raise our Mar’21 target price to Rs 690 (from Rs 570), based on a 14x (earlier 12x) EV/EBITDA multiple on Mar’22E – this represents an implied P/E of 28x. Our target valuation multiple is 10% lower than the midpoint of the eight-year historical band (11-21x). The increase in multiple is to factor in a resilient business model (relatively lower impact from Covid-19), backed by a stable domestic formulation market and supportive global generic environment amidst the virus-led disruption. Intensity of US generic pricing pressure is also easing.

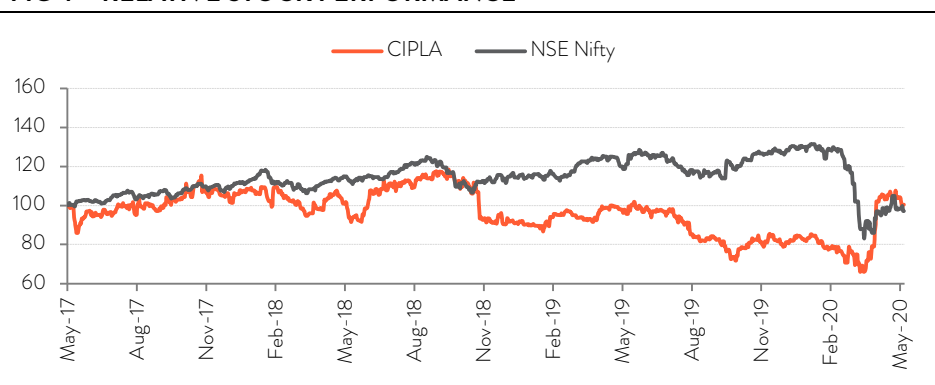
We marginally tweak our FY21-FY22 EPS estimates and continue to expect a core EPS CAGR of 15-18% over FY20-FY22. Advair approval represents an upside risk to our EPS estimates.

FIG 3 – REVISED ESTIMATES

(Rs bn)	New			Old			Change (%)		
	FY20P	FY21E	FY22E	FY20E	FY21E	FY22E	FY20P	FY21E	FY22E
Sales	171	178	192	170	179	193	0.9	(0.7)	(0.4)
EBITDA	33	34	38	33	35	39	(1.8)	(1.6)	(1.0)
EBITDA margin (%)	19.0	19.3	19.9	19.5	19.5	20.1	(52bps)	(18bps)	(12bps)
EPS (Rs)	20	22	25	20	21.9	25	(1.2)	(1.4)	(1.3)

Source: Company, BOBCAPS Research

FIG 4 – 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 the ramp up of key launches like Proventil HFA and Flonase launch 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	FY20P	FY21E	FY22E
Total revenue	152,181	163,621	171,243	178,060	191,896
EBITDA	28,254	30,973	32,574	34,388	38,265
Depreciation	13,228	13,263	11,760	12,893	13,924
EBIT	15,026	17,710	20,814	21,495	24,341
Net interest income/(expenses)	(1,142)	(1,684)	(1,972)	(1,144)	(715)
Other income/(expenses)	984	2,915	3,331	3,517	3,629
Exceptional items	0	0	0	0	0
EBT	14,868	18,941	22,173	23,868	27,255
Income taxes	2,501	5,696	6,310	6,444	7,359
Extraordinary items	1,817	1,850	0	0	0
Min. int./Inc. from associates	27	(181)	5	0	0
Reported net profit	14,157	15,277	15,858	17,424	19,896
Adjustments	1,817	1,850	0	0	0
Adjusted net profit	12,340	13,426	15,858	17,424	19,896

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Accounts payables	21,191	19,480	25,013	24,677	26,632
Other current liabilities	7,904	10,126	9,960	10,393	11,216
Provisions	7,650	8,582	8,919	9,307	10,045
Debt funds	40,980	43,161	28,160	17,600	11,000
Other liabilities	0	0	0	0	0
Equity capital	1,610	1,611	1,613	1,613	1,613
Reserves & surplus	147,378	154,016	167,461	182,465	199,943
Shareholders' fund	148,988	155,627	169,073	184,078	201,555
Total liabilities and equities	226,713	236,976	241,125	246,055	260,448
Cash and cash eq.	9,655	6,188	9,630	14,788	25,587
Accounts receivables	31,020	41,507	38,910	37,965	38,412
Inventories	40,450	39,648	43,204	45,083	48,655
Other current assets	23,697	21,866	23,239	24,250	26,171
Investments	12,586	25,539	25,539	25,539	25,539
Net fixed assets	53,154	51,144	48,053	46,967	45,794
CWIP	9,813	6,762	8,245	8,245	8,245
Intangible assets	46,337	44,322	44,305	43,219	42,046
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	226,712	236,976	241,125	246,055	260,448

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20P	FY21E	FY22E
Net income + Depreciation	27,385	28,540	27,618	30,316	33,820
Interest expenses	1,142	1,684	1,972	1,144	715
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(9,765)	(6,412)	3,373	(1,459)	(2,424)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	18,761	23,812	32,963	30,001	32,111
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	1	0	0
Debt raised/repaid	(146)	2,181	(15,001)	(10,560)	(6,600)
Interest expenses	(1,142)	(1,684)	(1,972)	(1,144)	(715)
Dividends paid	(1,609)	(2,417)	(2,419)	(2,419)	(2,419)
Other financing cash flows	7,775	(6,181)	801	1,086	1,173
Cash flow from financing	4,879	(8,099)	(18,590)	(13,037)	(8,561)
Changes in cash and cash eq.	3,415	(3,468)	3,441	5,158	10,799
Closing cash and cash eq.	9,656	6,187	9,629	14,788	25,587

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20P	FY21E	FY22E
Reported EPS	17.6	19.0	19.7	21.6	24.7
Adjusted EPS	15.3	16.7	19.7	21.6	24.7
Dividend per share	3.0	3.0	3.0	3.0	3.0
Book value per share	180.4	188.9	205.6	224.2	245.9

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20P	FY21E	FY22E
EV/Sales	3.2	3.0	2.8	2.6	2.3
EV/EBITDA	17.4	15.6	14.7	13.6	11.7
Adjusted P/E	37.2	34.2	29.0	26.4	23.1
P/BV	3.2	3.0	2.8	2.5	2.3

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20P	FY21E	FY22E
Tax burden (Net profit/PBT)	83.0	70.9	71.5	73.0	73.0
Interest burden (PBT/EBIT)	98.9	107.0	106.5	111.0	112.0
EBIT margin (EBIT/Revenue)	9.9	10.8	12.2	12.1	12.7
Asset turnover (Revenue/Avg TA)	20.8	21.0	21.6	22.3	23.2
Leverage (Avg TA/Avg Equity)	1.3	1.3	1.2	1.2	1.1
Adjusted ROAE	8.9	9.0	10.0	10.1	10.5

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

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20P	FY21E	FY22E
YoY growth (%)					
Revenue	4.1	7.5	4.7	4.0	7.8
EBITDA	14.9	9.6	5.2	5.6	11.3
Adjusted EPS	(0.2)	8.8	18.1	9.9	14.2
Profitability & Return ratios (%)					
EBITDA margin	18.6	18.9	19.0	19.3	19.9
EBIT margin	9.9	10.8	12.2	12.1	12.7
Adjusted profit margin	8.1	8.2	9.3	9.8	10.4
Adjusted ROAE	8.9	9.0	10.0	10.1	10.5
ROCE	8.7	10.6	12.2	12.5	13.5
Working capital days (days)					
Receivables	77	95	86	80	75
Inventory	100	91	95	95	95
Payables	52	45	55	52	52
Ratios (x)					
Gross asset turnover	1.2	1.2	1.2	1.1	1.1
Current ratio	2.9	2.9	2.6	2.8	2.9
Net interest coverage ratio	13.2	10.5	10.6	18.8	34.0
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%

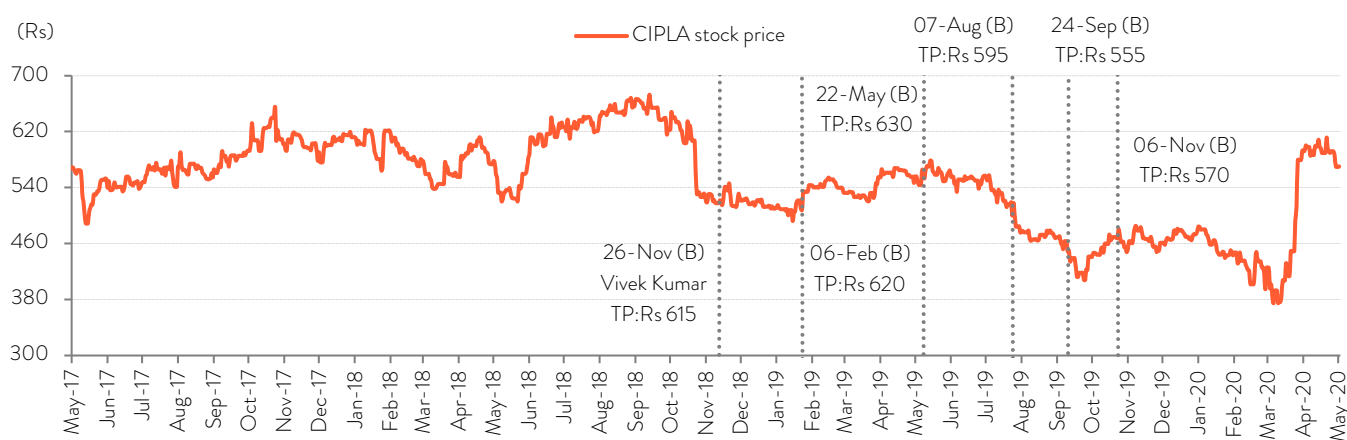
ADD – Expected return from >+5% to +15%

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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