

ADD

TP: Rs 840 | ▲ 9%

LUPIN

Pharmaceuticals

07 November 2019

Q2 a slight miss; US to improve in H2

Core Q2 EBITDA, normalised for licensing income, was a 5% miss at Rs 6bn (flat QoQ). Regional sales mix was 3% below estimate. US sales were stable at US\$ 189mn; management expects a robust H2 aided by the Levothyroxine franchise and four injectable launches in Q4. Capacity expansion in Levo will come in early next year but ramp-up is ahead of schedule, per Lupin (LPC). While FY21 growth drivers are on track, the gProventil launch has been moved to H1FY21. Goa/Somerset site reinspection is expected by Q4. Retain ADD.

Vivek Kumar

research@bobcaps.in

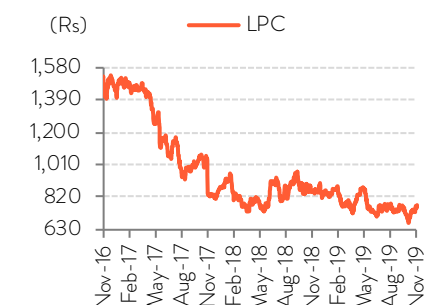
Base margins down QoQ; US sales to improve in H2: While core EBITDA was flat QoQ, the base margin at 14.2% (ex-licensing income) fell 150bps. Near-term margin gains appear unlikely given an expected increase in R&D spend (~10% of sales). Substantial operating leverage from US business (full-year impact of Levo, inj. portfolio, Solosec, gProAir) and cost control will be visible from FY21. LPC continues to target 20% share in Levo by Mar'20 (<5% now) and +65% gross margin. We expect US\$ 440mn in US sales in H2 (\$409mn in H1).

Ticker/Price	LPC IN/Rs 771
Market cap	US\$ 4.9bn
Shares o/s	453mn
3M ADV	US\$ 14.7mn
52wk high/low	Rs 906/Rs 646
Promoter/FPI/DII	47%/25%/12%

Source: NSE

Earnings call takeaways: (1) US\$ 150mn peak sales target on Solosec retained. (2) Expects to launch gEnbrel in Q1FY21 in the EU. (3) gProAir launch moved from Q4FY20 to H1FY21. (4) Second price cut likely in Japan in Dec'19, with focus on cost optimisation as market remains under pressure. (5) Settlement provision of US\$ 53.4mn relates to sales made prior to 2012. (6) US branded sales were US\$ 5mn, flat QoQ. (7) 20 launches in the US/filing rate of 25-30 ANDAs planned for FY21. (8) Levo price erosion lower than traditional drugs.

STOCK PERFORMANCE



Source: NSE

Maintain ADD: We retain our FY21/FY22 EPS estimates and believe the stock is partly pricing in expected EPS growth of 22% over the next two years – hence, maintain ADD with a TP of 840 (12x Sep'21E EV/EBITDA).

KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue (Rs mn)	158,021	167,010	177,435	196,191	210,728
EBITDA (Rs mn)	31,453	27,020	30,142	35,304	39,624
Adj. net profit (Rs mn)	17,137	9,464	10,319	14,809	17,125
Adj. EPS (Rs)	37.9	20.9	22.8	32.7	37.8
Adj. EPS growth (%)	(41.5)	(44.8)	9.0	43.5	15.6
Adj. ROAE (%)	12.6	6.9	7.4	10.3	11.3
Adj. P/E (x)	20.4	36.9	33.8	23.6	20.4
EV/EBITDA (x)	12.7	14.9	13.2	11.4	10.1

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q2FY20	Q2FY19	YoY (%)	Q1FY20	QoQ (%)	Q2FY20E	Var. (%)
Net Sales	43,596	39,510	10.3	44,183	(1.3)	44,867	(2.8)
EBITDA	7,313	5,496	33.1	8,603	(15.0)	7,647	(4.4)
Depreciation	3,214	2,655	-	3,171	-	2,974	-
EBIT	4,099	2,841	44.3	5,432	(24.5)	4,673	-
Interest	864	738	-	856	-	738	-
Other Income	1,332	2,306	-	822	-	600	-
PBT	4,567	4,409	3.6	5,398	(15.4)	4,535	-
Less: Taxation	343	1,729	-	2,280	-	1,587	-
Less: Minority Interest	0	(25)	-	88	-	0	-
Recurring PAT	4,224	2,705	56.2	3,030	39.4	2,948	43.3
Exceptional items	(5,464)	0	-	0	-	0	-
Reported PAT	(1,240)	2,705	(145.8)	3,030	(140.9)	2,948	(142.1)
Key Ratios (%)							
Gross Margin	65.0	64.7	-	64.9	-	65.0	-
EBITDA Margin	16.8	13.9	-	19.5	-	17.0	-
Tax / PBT	7.5	39.2	-	42.2	-	35.0	-
NPM	9.7	6.8	-	6.9	-	6.6	-
EPS (Rs)	9.3	6.0	-	6.7	-	6.5	-

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q2FY20	Q2FY19	YoY (%)	Q1FY20	QoQ (%)	Q2FY20E	Var. (%)
Formulations	38,476	35,562	8.2	40,069	(4.0)	39,086	(1.6)
US	13,244	12,487	6.1	15,412	(14.1)	13,510	(2.0)
India	13,419	12,032	11.5	13,077	2.6	13,600	(1.3)
APAC	6,352	6,199	2.5	6,717	(5.4)	6,323	0.5
EMEA	3,196	2,949	8.4	2,604	22.7	3,539	(9.7)
LATAM	1,445	1,459	(1.0)	1,550	(6.8)	1,634	(11.6)
RoW	820	436	88.1	709	15.7	480	71.0
APIs	3,052	3,347	(8.8)	3,489	(12.5)	3,682	(17.1)
Other Operating income	2,069	601	244.3	625	231.0	2,100	(1.5)
Net Sales	43,597	39,510	10.3	44,183	(1.3)	44,867	(2.8)

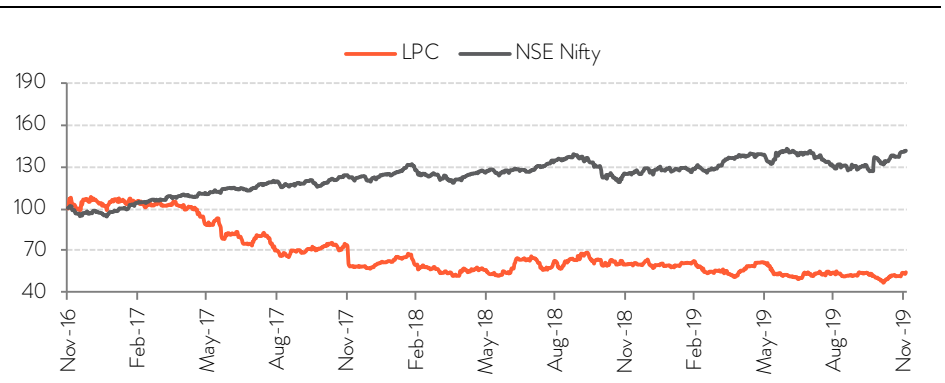
Source: Company, BOBCAPS Research

Valuation methodology

At CMP, Lupin is trading at 23x FY21E EPS which is reasonable and largely pricing in the earnings pick-up expected over the next two years. We forecast 22% EPS growth over FY19-FY22, building in gProAir and gBrovana in FY21. We have not penciled in upsides from distant opportunities gSpiriva (FY23 US launch) and gEnbrel (FY22 EU opportunity, in our view).

Retain ADD with an unchanged Sep'20 price target of Rs 840, based on an EV/EBITDA multiple of 12x Sep'21E (implied P/E of 24x). A deepening US product pipeline, Japan business exit and high share of branded generics are other key long-term positives.

FIG 3 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Upside risks

- Earlier-than-expected resolution of warning letters at Goa and Indore Unit II – together both events have the potential to increase FY21E EBITDA by 10%.
- gSpiriva (FY23 US launch) and gEnbrel (FY22 EU launch).

Downside risks

- Higher-than-expected price erosion in the US.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Total revenue	158,021	167,010	177,435	196,191	210,728
EBITDA	31,453	27,020	30,142	35,304	39,624
Depreciation	10,857	10,850	12,226	13,277	14,329
EBIT	20,596	16,170	17,916	22,026	25,295
Net interest income/(expenses)	(2,043)	(3,078)	(2,960)	(2,865)	(2,789)
Other income/(expenses)	1,504	5,441	2,359	2,124	2,125
Exceptional items	0	0	0	0	0
EBT	20,057	18,533	17,315	21,286	24,631
Income taxes	2,885	9,017	6,926	6,386	7,389
Extraordinary items	(14,643)	(3,399)	0	0	0
Min. int./Inc. from associates	36	52	70	91	117
Reported net profit	2,494	6,065	10,319	14,809	17,125
Adjustments	14,643	3,399	0	0	0
Adjusted net profit	17,137	9,464	10,319	14,809	17,125

Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Accounts payables	24,754	23,935	26,602	28,726	30,393
Other current liabilities	18,886	23,386	23,386	23,386	23,386
Provisions	8,085	11,807	9,623	12,138	13,727
Debt funds	68,762	82,219	79,059	76,530	74,508
Other liabilities	0	0	0	0	0
Equity capital	904	905	905	905	905
Reserves & surplus	135,667	136,985	138,377	146,532	155,963
Shareholders' fund	136,571	137,890	139,282	147,437	156,868
Total liabilities and equities	257,058	279,237	277,951	288,218	298,882
Cash and cash eq.	14,080	9,872	4,008	4,034	7,762
Accounts receivables	51,922	51,498	54,938	60,745	65,246
Inventories	36,624	38,368	39,836	44,047	47,311
Other current assets	22,484	29,534	30,534	31,534	32,534
Investments	2,348	22,703	21,099	21,099	21,099
Net fixed assets	79,136	87,064	86,838	85,561	83,232
CWIP	25,981	16,396	16,896	17,396	17,896
Intangible assets	24,484	23,803	23,803	23,803	23,803
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	257,059	279,237	277,951	288,218	298,882

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Net income + Depreciation	23,847	17,539	22,545	28,086	31,454
Interest expenses	2,043	3,078	2,960	2,865	2,789
Non-cash adjustments	(2,465)	290	0	0	0
Changes in working capital	(3,352)	(994)	(5,425)	(6,379)	(5,509)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	20,073	19,913	20,079	24,573	28,734
Capital expenditures	(19,298)	(9,136)	(12,500)	(12,500)	(12,500)
Change in investments	19,013	(20,355)	1,604	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(285)	(29,490)	(10,896)	(12,500)	(12,500)
Equities issued/Others	1	1	0	0	0
Debt raised/repaid	(10,758)	13,457	(3,160)	(2,528)	(2,023)
Interest expenses	(2,043)	(3,078)	(2,960)	(2,865)	(2,789)
Dividends paid	(4,651)	(7,274)	(4,636)	(6,653)	(7,694)
Other financing cash flows	4,748	2,264	(4,291)	0	0
Cash flow from financing	(12,703)	5,369	(15,048)	(12,047)	(12,506)
Changes in cash and cash eq.	7,085	(4,208)	(5,864)	26	3,728
Closing cash and cash eq.	14,079	9,872	4,008	4,034	7,762

Per Share

Y/E 31 Mar (Rs)	FY18A	FY19A	FY20E	FY21E	FY22E
Reported EPS	5.5	13.4	22.8	32.7	37.8
Adjusted EPS	37.9	20.9	22.8	32.7	37.8
Dividend per share	9.0	6.0	10.2	14.7	17.0
Book value per share	300.9	303.7	306.8	324.8	345.6

Valuations Ratios

Y/E 31 Mar (x)	FY18A	FY19A	FY20E	FY21E	FY22E
EV/Sales	2.5	2.4	2.2	2.1	1.9
EV/EBITDA	12.7	14.9	13.2	11.4	10.1
Adjusted P/E	20.4	36.9	33.8	23.6	20.4
P/BV	2.6	2.5	2.5	2.4	2.2

DuPont Analysis

Y/E 31 Mar (%)	FY18A	FY19A	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	85.4	51.1	59.6	69.6	69.5
Interest burden (PBT/EBIT)	97.4	114.6	96.6	96.6	97.4
EBIT margin (EBIT/Revenue)	13.0	9.7	10.1	11.2	12.0
Asset turnover (Revenue/Avg TA)	15.3	15.6	15.9	17.3	17.9
Leverage (Avg TA/Avg Equity)	1.9	2.0	2.0	2.0	1.9
Adjusted ROAE	12.6	6.9	7.4	10.3	11.3

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

Ratio Analysis

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
YoY growth (%)					
Revenue	(9.7)	5.7	6.2	10.6	7.4
EBITDA	(35.4)	(14.1)	11.6	17.1	12.2
Adjusted EPS	(41.5)	(44.8)	9.0	43.5	15.6
Profitability & Return ratios (%)					
EBITDA margin	19.9	16.2	17.0	18.0	18.8
EBIT margin	13.0	9.7	10.1	11.2	12.0
Adjusted profit margin	10.8	5.7	5.8	7.5	8.1
Adjusted ROAE	12.6	6.9	7.4	10.3	11.3
ROCE	8.3	4.9	5.3	7.3	8.1
Working capital days (days)					
Receivables	110	113	113	113	113
Inventory	84	82	82	82	82
Payables	175	152	160	160	160
Ratios (x)					
Gross asset turnover	1.4	1.3	1.2	1.2	1.2
Current ratio	2.4	2.2	2.2	2.2	2.3
Net interest coverage ratio	10.1	5.3	6.1	7.7	9.1
Adjusted debt/equity	0.4	0.4	0.4	0.3	0.3

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

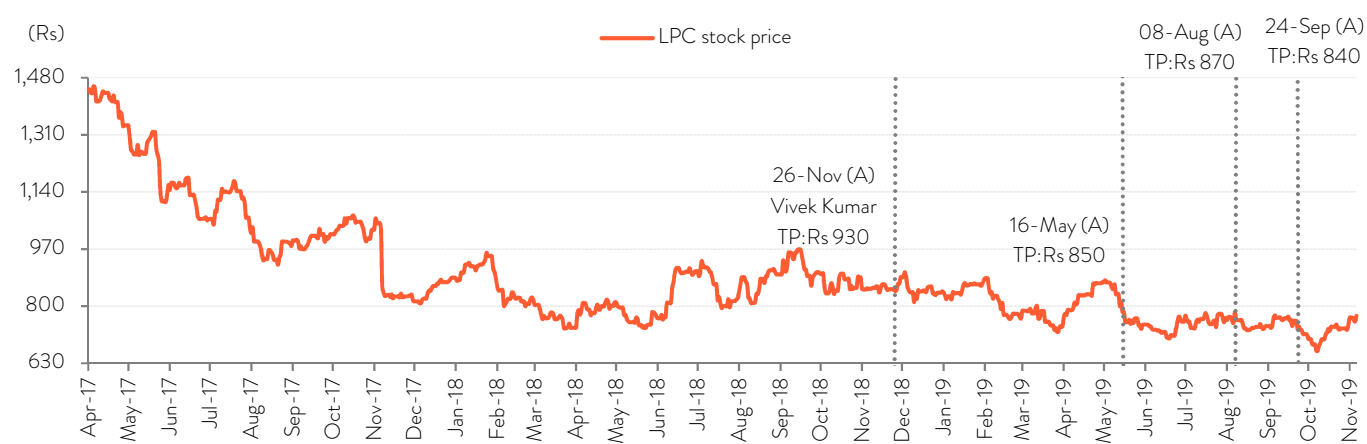
ADD – Expected return from >+5% to +15%

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: LUPIN (LPC IN)



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

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