

November 20, 2017

Cipla

Performance Highlights

Y/E March (₹ cr)	2QFY2018	1QFY2018	% chg qoq	2QFY2017	% chg yoy
Net sales	3,988	3,432	16.2	3,672	8.6
Other income	207	244	(15.0)	106	95.0
Gross profit	2,435	2,256	8.0	2,342	4.0
Operating profit	710	554	28.2	602	18.0
Adj. Net profit	422	409	3.3	354	19.2

Source: Company, Angel Research

Cipla posted lower than expected results on all fronts for 2QFY2018. In Rupee terms, revenues came in at ₹3,988cr v/s. ₹4,243cr expected, up 8.6% yoy. Domestic sales posted a growth of 10.2% yoy; while exports grew by 7.5% yoy. On the operating front, the EBITDA margin came in at 17.8% (19.7% expected) v/s. 16.4% in 2QFY2017; a yoy expansion of 140bps. Consequently, PAT came in at ₹422cr v/s. ₹499cr expected, a growth of 19.2% yoy. **We maintain our Sell rating.**

Results lower than our expectations: Sales came in at ₹3,988cr (₹4,243cr expected) v/s. ₹3,672cr in 2QFY2017, a yoy growth of 8.6%. Indian formulation sales posted (₹1,677cr) a yoy growth of 10.2%, while exports grew by 7.5% yoy. USA sales at US\$96mn, posted a yoy de-growth of 3.0%, South Africa, Sub-Saharan Africa and Cipla Access sales at US\$143mn, posted a growth of 9.0%. On operating front, the EBITDA margins came in at 17.8% (19.7% expected) v/s. 16.4% in 2QFY2017. Thus, the PAT came in at ₹422cr (₹499cr expected) v/s. ₹354cr in 2QFY2017, a yoy growth of 19.2%.

Outlook and valuation: We expect the company to post a 14.5% CAGR in net sales to ₹18,711cr and EPS to record a 39.3% CAGR to ₹24.3 over FY2017–19E. **We re-iterate our SELL stance on the stock.**

Key financials (Consolidated)

Y/E March (₹ cr)	FY2016	FY2017	FY2018E	FY2019E
Net sales	13,494	14,281	16,163	18,711
% chg	15.5	5.8	13.2	15.8
Adj. Net profit	1,360	1,006	1,665	1,953
% chg	(13.8)	(26.0)	65.4	17.3
EPS (₹)	16.9	12.5	20.7	24.3
EBITDA margin (%)	16.2	14.9	16.6	16.9
P/E (x)	36.0	48.6	29.4	25.0
RoE (%)	12.2	8.4	12.6	13.1
RoCE (%)	9.1	4.4	9.8	10.9
P/BV (x)	4.2	3.9	3.5	3.1
EV/Sales (x)	3.9	3.6	3.2	2.7
EV/EBITDA (x)	24.2	24.4	19.1	16.0

Source: Company, Angel Research; Note: CMP as of November 17, 2017

SELL

CMP	₹609
Target Price	₹462
Investment Period	-

Stock Info

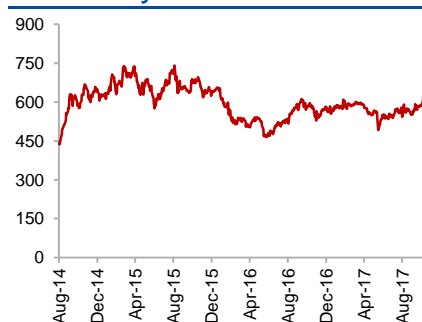
Sector	Pharmaceutical
Market Cap (₹ cr)	48,978
Net Debt (₹ cr)	3,488
Beta	0.7
52 Week High / Low	622/479
Avg. Daily Volume	69,441
Face Value (₹)	2
BSE Sensex	33,343
Nifty	10,284
Reuters Code	CIPL.BO
Bloomberg Code	CIPLA@IN

Shareholding Pattern (%)

Promoters	36.7
MF / Banks / Indian FIs	17.9
FII / NRIs / OCBs	26.9
Indian Public / Others	18.5

Abs. (%)	3m	1yr	3yr
Sensex	# 27.1	18.3	
Cipla	# 11.7	(0.7)	

3-Year Daily Price Chart



Source: Company, Angel Research

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Exhibit 1: 2QFY2018 (Consolidated) performance

Y/E March (` cr)	2QFY2018	1QFY2018	% chg qoq	2QFY2017	% chg yoy	1HFY2018	1HFY2017	% chg yoy
Net sales	3,988	3,432	16.2	3,672	8.6	7,421	7,228	2.7
Other income	207.5	244.1	(15.0)	106.4	95.0	451.6	225.5	100.3
Total income	4,196	3,676	14.1	3,778	11.0	7,872	7,454	5.6
Gross profit	2435	2256	8.0	2342	4.0	4691	4527	3.6
Gross margin	61.1	65.7		63.8		63.2	62.6	
Operating profit	710	554	28.2	602	18.0	1264	1119	12.9
OPM (%)	17.8	16.1		16.4		17.0	15.5	
Interest	42.0	27.9	50.8	35.2	19.5	70	67	4.3
Depreciation	302	213	41.6	229	31.9	516	433	19.1
PBT	573	557	3.0	444	29.2	1130	845	33.8
Provision for taxation	137	131	5.1	72	-	268	127	111.2
PAT before extra-ordinary item	436	426	2.3	372	17.2	862	718	20.1
Share of Profit /(loss) of asso.	13	17		15		29	20	
Extra-ordinary items/(income)				0		0	0	
PAT after extra-ordinary item	422	409	3.3	354	19.2	831	693	19.9
Adj. PAT	422	409	3.3	354	19.2	831	693	19.9
EPS (`)	5.3	5.1	3.3	4.4	19.2	10.3	8.6	19.9

Source: Company, Angel Research

Exhibit 2: 2QFY2018 – Actual vs. Angel estimates

(` cr)	Actual	Estimates	Variance
Net sales	3,988	4,243	(6.0)
Other income	207	106	95.0
Operating profit	710	837	(15.1)
Tax	137	159	(13.4)
Net profit	422	499	(15.4)

Source: Company, Angel Research

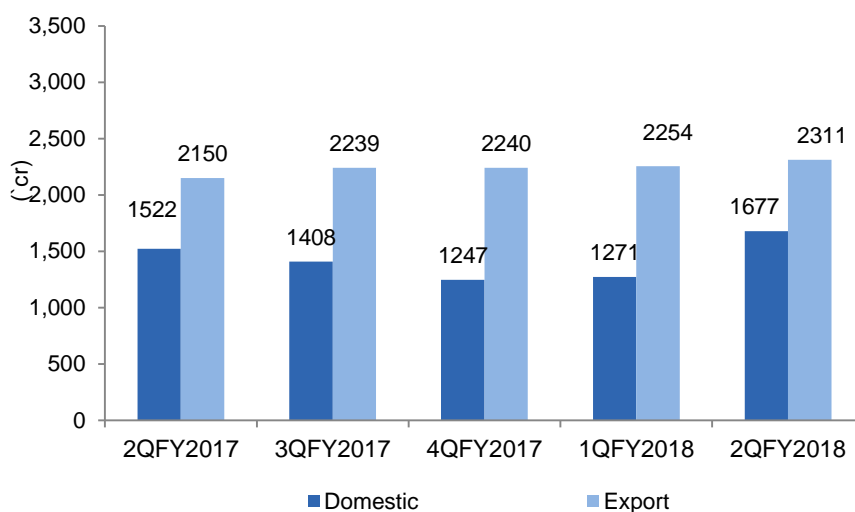
Top-line growth lower than expectation

Sales came in at `3,988cr (`4,243cr expected) v/s. `3,672cr in 2QFY2017, a yoy growth of 8.6%, mainly driven by Indian formulation sales. Indian formulation sales registered (`1,677cr) a yoy growth of 10.2%, while exports (`2,311cr) posted a yoy growth of 7.5%.

USA (US\$96mn) posted a yoy de-growth of 3% in \$ terms. Cipla is now one of the fastest growing generics players in the US, strong DTM performance i.e. 10 of the 47 (21%) in IMS are in the leadership (no 1) position; while 30 of 47 (64%) products ranked among Top 3 in their segments. 5 ANDAs have been filed, during the quarter, with 20-25 expected to be filed in FY2018.

South Africa (SA) (US\$143mn) registered a yoy growth of ~9% over the last year. As per IMS MAT (Sept'2017), Cipla grew at 11.3% in the private market v/s. 9.5% market growth. Cipla maintained its overall ranking in SA as the 4th largest pharmaceutical company, and including the tender business, Cipla is the 3rd largest pharmaceuticals company in SA. Emerging market sales (US\$71mn) posted a 15% yoy growth.

Exhibit 3: Sales Trend

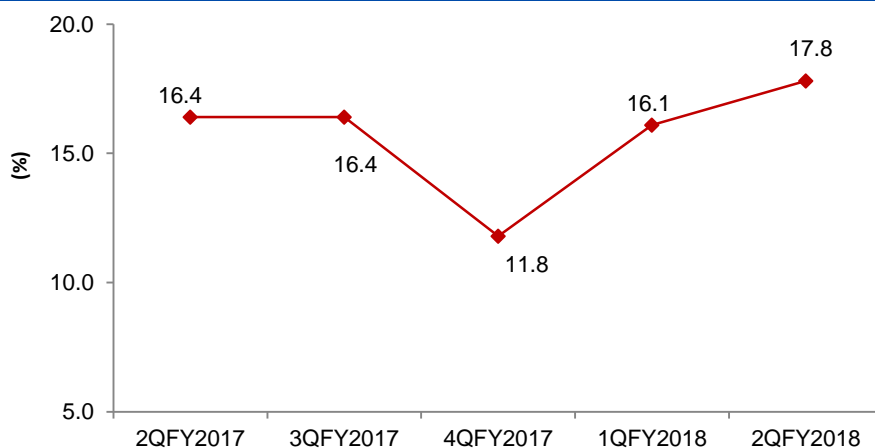


Source: Company

Operating profit margin lower than expectation

On operating front, the EBITDA margins came in at 17.8% (19.7% expected) v/s. 16.4% in 2QFY2017, mainly on the back of lower than expected sales during the quarter and 2.1% dip in the other expenses. Gross margins came in at 61.1% v/s. 63.8% in 2QFY2017.

Exhibit 4: OPM Trend

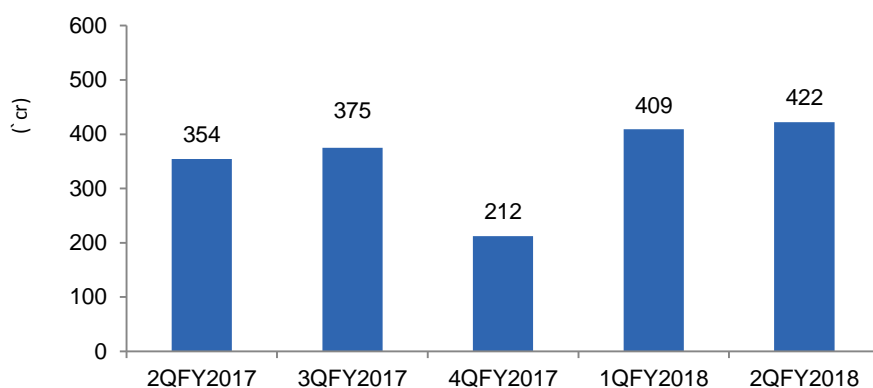


Source: Company

Net profit lower than expectation; aided by lower than expected OPM

Thus, the PAT came in at ` 422cr (`499cr expected) v/s. `354cr in 2QFY2017, a yoy growth of 19.2%. This was mainly on back of the lower than expected OPM. However, on yoy growth in the PAT was higher than sales growth on back of the expansion in the OPM. This was also aided by the other income during the quarter, which came in at `208cr v/s. `106cr during the last corresponding period. Also Tax as % of PBT was 23.6% and 16.0% in 2QFY2017.

Exhibit 5: Net Profit Trend



Source: Company

Concall Takeaways

- R&D is expected to remain at 8% in 2HFY2018E, and not more than 9% in coming years.
- On track to file 20-25 ANDAs in FY2018 (filed 8 in H1FY2018).
- Targets to improve EBITDA by 100 bps annually led by cost-saving initiatives.
- Tax rate expected to be 25% of PBT in FY2018E.
- Capex expected to be around `800-850cr in FY2018.

Recommendation rationale

Export segment to be the growth driver: Cipla exports to more than 180 countries, with growth coming through marketing alliances and distribution tie-ups in various markets. Exports contributed 60% to the total turnover in FY2017, with Africa, US and Latin America constituting more than ~60% of total exports. In the US, Cipla has a strong product pipeline of 238 ANDAs, out of which, 142 are approved. Another long term growth driver for the company is the launch of the CFC-free inhalers in the regulated markets. CFC-free inhalers in Europe and US address a potential market size of more than US\$3bn. Overall, we expect the company's exports to grow at a CAGR of 15.4% during FY2017-19E.

Increasing penetration in the domestic market: Cipla is one of the largest players in the domestic formulation market with a market share of around 5.3%. Domestic formulations contributed 40% to the company's total turnover in FY2017. The

company is the market leader in key therapeutic areas such as respiratory care, anti-viral and urological. Cipla's distribution network in India consists of a field force of around 7,000-8,000 employees. The company plans to increase its focus on domestic markets with new therapies such as oncology and neuro-psychiatry in the offing. The company plans to focus on growing its market share and sales by increasing penetration in the Indian market, especially in rural areas, and plans to expand its product portfolio by launching biosimilar, particularly related to the oncology, anti-asthmatic and anti-arthritis categories. Overall, we expect the company's domestic formulation business to post a CAGR of 13.0% over FY2017-19E.

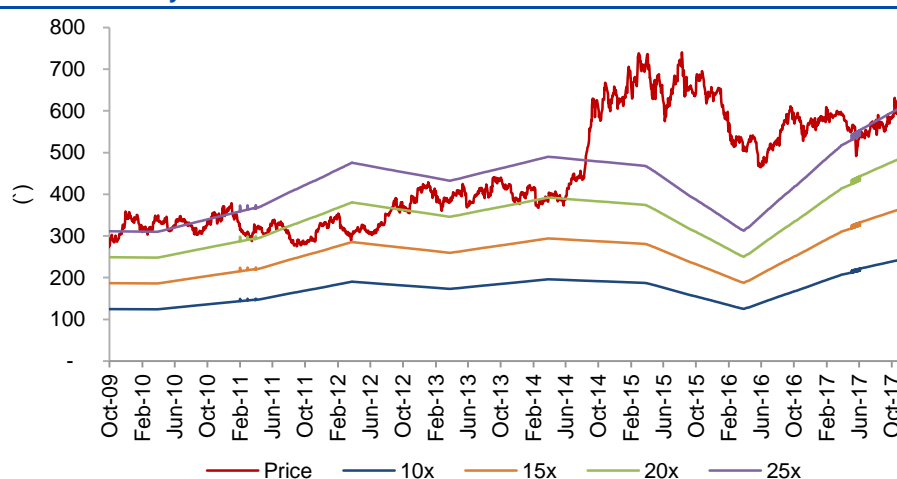
Valuation: We expect the company to post a 14.5% CAGR in net sales to `18,711cr and EPS to record a 39.3% CAGR to `24.3 over FY2017-19E. The growth in the top-line would be driven by domestic formulation sales and exports. **We maintain our SELL stance on the stock.**

Exhibit 6: Key assumptions

Key assumptions	FY2018E	FY2019E
Domestic growth (%)	12.0	14.0
Exports growth (%)	14.0	16.9
Growth in employee expenses (%)	15.0	15.0
Operating margins (excl tech. know-how fees) (%)	16.6	16.9

Source: Company, Angel Research

Exhibit 7: One-year forward PE band



Source: Company, Angel Research

Exhibit 8: Recommendation Summary

Company	Reco	CMP (₹)	Tgt. price (₹)	Upside (%)	PE (x)	EV/Sales (x)	FY2019E	FY17-19E	FY2019E	
							EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma	Buy	514	600	16.8	21.5	2.5	12.9	5.7	20.6	18.4
Aurobindo Pharma	Buy	708	823	16.3	13.8	2.1	9.6	14.2	25.3	22.7
Cadila Healthcare	Reduce	446	411	(7.9)	21.7	3.5	17.3	18.9	16.5	22.2
Cipla	Sell	609	426	(24.1)	25.0	2.7	16.0	39.3	10.9	13.1
Dr Reddy's	Reduce	2,325	2,040	(12.3)	22.8	2.8	13.7	18.5	10.8	12.4
Dishman Pharma	Under Review	301	-	-	19.3	2.7	11.5	23.3	4.5	4.4
GSK Pharma	Sell	2,511	2000	(20.4)	51.4	6.4	37.7	19.3	25.8	23.5
Indoco Remedies	Sell	267	153	(42.8)	16.7	2.1	14.9	16.2	10.1	14.5
Ipca labs	Neutral	529	-	-	22.1	1.7	11.2	24.7	12.4	11.0
Lupin	Buy	829	1,091	31.6	16.7	2.1	9.7	(6.6)	13.7	13.7
Sanofi India*	Neutral	4,485	-	-	27.4	3.2	17.1	12.8	25.8	27.5
Sun Pharma	Accumulate	517	558	7.9	20.9	3.5	15.4	(12.9)	12.3	15.2

Source: Company, Angel Research; Note: * December year ending

Company Background

Cipla is a leading pharmaceutical company in India with a strong presence in both, the export and domestic markets. On the exports front, where it follows the partnership model, it has 5,700 product registrations in around 180 countries. Cipla is a market leader in the domestic formulation market with ~5.3% market share. The company is likely to continue on the growth trajectory owing to its entry into the inhalers market in the EU and potential new long-term manufacturing contracts with Global Innovators.

Profit & loss statement (Consolidated)

Y/E March (` cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Gross sales	9,902	11,861	13,709	14,497	16,415	19,005
Less: Excise duty	149.3	179.7	215.0	216.4	251.8	294.5
Net sales	9,753	11,681	13,494	14,281	16,163	18,711
Other operating income	348	348	296	349	349	349
Total operating income	10,100	12,029	13,790	14,630	16,513	19,060
% chg	22.0	19.1	14.6	6.1	12.9	15.4
Total expenditure	7,967	9,612	11,310	12,154	13,477	15,544
Net raw materials	3,875	4,556	5,090	5,317	6,029	6,979
Other mfg costs	827	993	1,142	1,313	1,510	1,736
Personnel	1,543	2,083	2,434	2,634	3,029	3,483
Other	1,722	1,981	2,645	2,891	2,909	3,346
EBITDA	1,786	2,069	2,184	2,126	2,686	3,166
% chg	(11.0)	15.9	5.5	(2.6)	26.3	17.9
(% of Net Sales)	18.3	17.7	16.2	14.9	16.6	16.9
Depreciation & amort.	373	457	754	1,323	848	944
EBIT	1,413	1,613	1,430	803	1,839	2,223
% chg	(15.6)	14.1	(11.4)	(43.8)	128.8	20.9
(% of Net Sales)	14.5	13.8	10.6	5.6	11.4	11.9
Interest & other charges	146	85	207	159	159	159
Other Income	266	266	209	229	229	229
(% of PBT)	14.1	12.4	12.1	18.7	10.1	8.7
Recurring PBT	1,881	2,141	1,728	1,222	2,257	2,641
% chg	(9.1)	13.8	(19.3)	(29.3)	84.7	17.0
Extraordinary exp./ (Inc.)	-	-	-	-	-	-
PBT (reported)	1,881	2,141	1,728	1,222	2,257	2,641
Tax	463.4	535.3	331.6	179.8	564.3	660.3
(% of PBT)	24.6	25.0	19.2	14.7	25.0	25.0
PAT (reported)	1,417	1,606	1,396	1,042	1,693	1,981
Add: Share of earnings of asso.	(12)	(12)	(12)	(7)	(10)	(9)
Less: Minority interest (MI)	16	16	23	29	18	19
Prior period items	-	-	-	-	-	-
PAT after MI (reported)	1,388	1,578	1,360	1,006	1,665	1,953
ADJ. PAT	1,388	1,578	1,360	1,006	1,665	1,953
% chg	(8.9)	13.6	(13.8)	(26.0)	65.4	17.3
(% of Net Sales)	14.2	13.5	10.1	7.0	10.3	10.4
Basic EPS (`)	17.3	19.6	16.9	12.5	20.7	24.3
Fully Diluted EPS (`)	17.3	19.6	16.9	12.5	20.7	24.3
% chg	(8.9)	13.6	(13.8)	(26.0)	65.4	17.3

Balance sheet (Consolidated)

Y/E March (` cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
SOURCES OF FUNDS						
Equity share capital	161	161	161	161	161	161
Preference Capital	-	-	-	-	-	-
Reserves & surplus	9,890	10,629	11,356	12,365	13,841	15,606
Shareholders funds	10,050	10,801	11,516	12,525	14,002	15,767
Minority interest	50	180	350	438	438	438
Total loans	1,247.9	1,701.8	5,191.4	4,112.6	4,112.6	4,112.6
Other long term liabilities	32.6	32.6	32.6	32.6	32.6	32.6
Long Term Provisions	77.4	168.4	255.6	263.5	263.5	263.5
Deferred tax liability	309.0	284.6	897.0	588.8	588.8	588.8
Total liabilities	11,767	13,169	18,243	17,961	19,438	21,202
APPLICATION OF FUNDS						
Gross block	6,183	6,868	8,293	9,999	11,199	12,399
Less: acc. depreciation	2,180	2,634	3,388	4,711	5,559	6,503
Net block	4,003	4,234	4,905	5,288	5,640	5,896
Capital work-in-progress	442	442	442	442	442	442
Goodwill	2,493	2,735	6,084	5,427	5,427	5,427
Investments	709	640	757	973	973	973
Long Term Loans and Adv.	301	419	603	773	874	1,012
Current assets	5,340	7,201	8,259	7,900	9,314	11,194
Cash	175	564	871	624	1,071	1,652
Loans & advances	596	701	958	857	970	1,123
Others	4,569	5,936	6,429	6,419	7,274	8,420
Current liabilities	1,634	2,501	2,806	2,841	3,233	3,742
Net current assets	3,706	4,700	5,453	5,059	6,082	7,452
Mis. Exp. not written off	112	-	-	-	-	-
Total assets	11,767	13,169	18,243	17,961	19,438	21,202

Cash flow statement (Consolidated)

Y/E March (` cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Profit before tax	1,881	2,141	1,728	1,222	2,257	2,641
Depreciation	373	457	754	1,323	848	944
(Inc)/Dec in Working Capital	(149)	(722)	(629)	(23)	(678)	(927)
Direct taxes paid	431	537	632	-	-	-
Cash Flow from Operations	1,673	1,339	1,221	2,522	2,427	2,658
(Inc.)/Dec.in Fixed Assets	(930)	(684)	(1,426)	(1,706)	(1,200)	(1,200)
(Inc.)/Dec. in Investments	1,824	69	(117)	(216)	-	-
Other income	-	-	-	-	-	-
Cash Flow from Investing	894	(616)	(1,543)	(1,922)	(1,200)	(1,200)
Issue of Equity	-	-	-	-	-	-
Inc./Dec.) in loans	311	545	3,577	(1,071)	-	-
Dividend Paid (Incl. Tax)	(188)	(188)	(188)	(188)	(188)	(188)
Others	(2,658)	(692)	(2,760)	412	(592)	(689)
Cash Flow from Financing	(2,535)	(335)	629	(847)	(780)	(877)
Inc./Dec.) in Cash	32	389	307	(247)	447	581
Opening Cash balances	143	175	564	871	624	1,071
Closing Cash balances	175	564	871	624	1,071	1,652

Key Ratio

Y/E March	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Valuation Ratio (x)						
P/E (on FDEPS)	35.2	31.0	36.0	48.6	29.4	25.0
P/CEPS	27.7	24.0	23.1	21.0	19.5	16.9
P/BV	4.9	4.5	4.2	3.9	3.5	3.1
Dividend yield (%)	0.3	0.3	0.3	0.3	0.3	0.3
EV/Sales	5.1	4.3	3.9	3.6	3.2	2.7
EV/EBITDA	27.8	24.0	24.2	24.4	19.1	16.0
EV / Total Assets	4.2	3.8	2.9	2.9	2.6	2.4
Per Share Data (₹)						
EPS (Basic)	17.3	19.6	16.9	12.5	20.7	24.3
EPS (fully diluted)	17.3	19.6	16.9	12.5	20.7	24.3
Cash EPS	21.9	25.3	26.3	29.0	31.3	36.1
DPS	2.0	2.0	2.0	2.0	2.0	2.0
Book Value	125.2	134.5	143.3	155.9	174.3	196.3
Dupont Analysis						
EBIT margin	14.5	13.8	10.6	5.6	11.4	11.9
Tax retention ratio	75.4	75.0	80.8	85.3	75.0	75.0
Asset turnover (x)	0.9	1.0	0.9	0.8	0.9	1.0
ROIC (Post-tax)	10.1	10.3	7.9	4.0	7.9	9.0
Cost of Debt (Post Tax)	9.9	4.3	4.8	2.9	2.9	2.9
Leverage (x)	0.1	0.0	0.0	1.0	2.0	3.0
Operating ROE	10.1	10.3	7.9	5.2	17.9	27.1
Returns (%)						
ROCE (Pre-tax)	12.8	12.9	9.1	4.4	9.8	10.9
Angel ROIC (Pre-tax)	15.3	17.8	14.1	7.2	15.3	17.0
ROE	14.6	15.1	12.2	8.4	12.6	13.1
Turnover ratios (x)						
Asset Turnover (Gross Block)	1.8	1.8	1.8	1.6	1.6	1.6
Inventory / Sales (days)	95	96	100	87	91	94
Receivables (days)	60	74	58	66	69	72
Payables (days)	41	55	73	49	51	51
WC cycle (ex-cash) (days)	124	116	115	112	104	104
Solvency ratios (x)						
Net debt to equity	0.1	0.1	0.4	0.3	0.2	0.2
Net debt to EBITDA	0.6	0.5	2.0	1.6	1.1	0.8
Interest Coverage (EBIT/Int.)	-	-	-	-	-	-

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Ratings (Based on expected returns over 12 months investment period):

Buy (> 15%)

Accumulate (5% to 15%)
Reduce (-5% to -15%)

Neutral (-5 to 5%)
Sell (< -15)