

May 16, 2018

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Rating	<b>Reduce</b>
Price	Rs751
Target Price	Rs727
Implied Upside	-3.2%
Sensex	35,544
Nifty	10,802

(Prices as on May 15, 2018)

### Trading data

Market Cap. (Rs bn)	339.5
Shares o/s (m)	452.1
3M Avg. Daily value (Rs m)	1180.7

### Major shareholders

Promoters	47.21%
Foreign	25.39%
Domestic Inst.	12.01%
Public & Other	15.40%

### Stock Performance

(%)	1M	6M	12M
Absolute	(3.9)	(8.7)	(41.5)
Relative	(7.9)	(17.2)	(58.8)

### How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2019	34.2	38.8	-11.7
2020	39.3	48.6	-19.2

### Price Performance (RIC: LUPN.BO, BB: LPC IN)



Source: Bloomberg

■ **US, Japan lacks growth drivers, India remain mediocre:** Lupin reported tepid results, while the trajectory was in line with our estimates, the results were even lower than our estimates. Lupin's sales, adj. EBITDA and adj. PAT in Q4FY18 decreased by 4%, 5% and 6% YoY respectively on strong decline in key products in US, price ceiling in Japan and moderate growth in India. India and EU-EMEA grew 10% and 17% YoY while US declined (in local currency) at 19% YoY. Adj. EBITDA margin was 16.4%, down by 700bps QoQ due to a) adverse portfolio mix of US generics, b) competitive growth in India sales and c) higher overheads. With ongoing price erosion led by consolidation of channel partners, there have been strong price erosion and loss of market share in key drugs of Lupin (gGlumetza, gFortamet and gMinastrin) in US, which are predominantly limited competition drugs. Lupin's sales in US were driven by a) launch of limited competition drugs gTamiflu suspension, gAxiron, gFosrenol and Vigamox b) seasonal sales of Suprax and c) peak sales of Methergin. Lupin guided for controlled R&D expenditures of Rs18.5-20bn in FY19E, flat growth in comparison to the R&D expenditure in FY18.

■ **Guided for 10 key launches in US though margin guidance remain tepid:** Management guided for 10 key launches in US in FY19E including Levothyroxin, gRanexa, gAxiron, gNamenda XR and NDA product Solosec. It expects seasonal benefits (good flu season in winter) and lower competition of gTamiflu (especially in Q4FY18) to be absent in FY19E. Lupin plans for expansion of its US sales force headcount from 70 to 125 before launch of branded Solosec in women healthcare segment in FY19.

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### Key financials (Y/e March)

	2017	2018	2019E	2020E
Revenues (Rs m)	171,198	155,598	166,214	182,044
Growth (%)	24.4	(9.1)	6.8	9.5
EBITDA (Rs m)	41,186	29,032	31,581	36,409
PAT (Rs m)	25,575	17,156	15,474	17,767
EPS (Rs)	56.6	37.9	34.2	39.3
Growth (%)	12.9	(33.0)	(9.8)	14.8
Net DPS (Rs)	7.5	7.5	7.5	7.5

### Profitability & Valuation

	2017	2018	2019E	2020E
EBITDA margin (%)	24.1	18.7	19.0	20.0
RoE (%)	20.7	12.7	11.1	11.8
RoCE (%)	12.9	8.5	7.7	8.7
EV / sales (x)	2.3	2.5	2.3	2.1
EV / EBITDA (x)	9.5	13.5	12.1	10.4
PE (x)	13.3	19.8	21.9	19.1
P / BV (x)	2.5	2.5	2.4	2.2
Net dividend yield (%)	1.0	1.0	1.0	1.0

Source: Company Data; PL Research

- **Valuation—Maintain “Reduce”, TP reduce to Rs727:** While launches of key para-IV drugs are positive development for US generics, it is not expected to be sustained in revenue growth and margin as USFDA increase approvals to multiple generics on a single molecule. This has led to guidance of lower gross margin by 100-150bps in FY19E. Lupin guided for price decline of high-single digit in US though expect turnaround from price erosion could be in the offing in medium term. While It guided EBITDA margin of 19-21%, it would be highly unlikely that Lupin achieve its guidance as US contributes 60% of EBITDA. While we maintain the sales estimates where increased volumes from newer launches will make up for fall in prices of existing products, we expect the margins to remain depressed leading to a decrease in EBITDA by 16% and 12% in FY19E and FY20E respectively. The stock currently trades at PER of 17.8x and 16.7x FY19E and FY20E, respectively and we reduce our TP to Rs727 (from earlier LupRs866) on 18.5x PE of FY20. We maintain our ‘Reduce’ recommendation.

### Key takeaways from Analyst Call

- US sales increased 5% QoQ US\$224m aided by new product launches (including Tamiflu). Lupin continues to witness price erosion in base portfolio. Management guided that they are close to bottoming out with respect to price erosion and expect prices to stabilize going forward.
- Management guided for launch of Solosec in US in June 2018. Lupin expects Methergine to go generic in Q1FY19E which can have an impact on gross margins going forward.
- Lupin expects to file 25-26 ANDAs in FY19E. Management expects to launch Solosec, Levothyroxine and Ranexa FY19E which we believe will partially offset the declining base business US revenues. Management guided for EBITDA margins to remain under pressure for the first quarter with increasing promotional costs for launch of Solosec and declining gross margins due to genericisation of Methergine
- Lupin expects to file Tiotropium with USFDA by Q1FY19E. On having missed out on first wave of products, management guided that they are in initial stages of development for 20-25 biosimilar products. Management guided to file Eterncept in EU in FY19E and US in Q4FY20E
- Management guided on building its portfolio with increased focus on Woman Healthcare in US and CNS in EU & Japan
- Management guided for South African business to grow at 20% in FY19E
- Adjusting for excise duty, India formulation sales grew 11% YoY whereas API sales declined by 1.6% YoY. Management guided for 16-17% growth in domestic formulation sales in FY19E
- R&D expenses were at 10% in Q4FY18 at Rs4bn and management guided to maintain similar R&D expenses in FY19E and FY20E despite requirements of

phase-III clinical with limited scope in key anti-asthma inhalers including Spiriva and Advair in near to medium term

- Working capital days increased from 134 days in FY17 to 138 days in FY18. Lupin incurred capex of Rs10.5bn in FY18 and guided for capex of Rs15bn in FY19E
- Lupin guided for single digit growth in overall revenues in FY19E with an aspirational EBITDA margin of 19-21% on the back of various cost reduction programmes

#### Exhibit 1: Change in Estimates

Year	Sales (Rs m)			EBITDA (Rs m)			PAT (Rs m)		
	Old	New	Diff (%)	Old	New	Diff (%)	Old	New	Diff (%)
FY19E	166,937	166,214	(0.4)	37,560	31,581	(15.9)	20,221	15,474	(23.5)
FY20E	182,835	182,044	(0.4)	41,140	36,409	(11.5)	21,640	17,767	(17.9)

Source: PL Research

#### Exhibit 2: Q4FY18 Result Overview (Rs m)

Y/e March	Q4FY18	Q4FY17	YoY gr. (%)	Q3FY18	FY18	FY17	YoY gr. (%)
<b>Net Sales</b>	<b>39,785</b>	<b>41,619</b>	<b>(4.4)</b>	<b>39,004</b>	<b>155,598</b>	<b>171,198</b>	<b>(9.1)</b>
Raw Material	13,626	11,851	15.0	13,927	52,744	50,014	5.5
<i>% of Net Sales</i>	<i>34.2</i>	<i>28.5</i>		<i>35.7</i>	<i>33.9</i>	<i>29.2</i>	
Personnel Cost	7,287	7,078	3.0	6,931	28,647	28,495	0.5
<i>% of Net Sales</i>	<i>18.3</i>	<i>17.0</i>		<i>17.8</i>	<i>18.4</i>	<i>16.6</i>	
Others	12,338	15,791	(21.9)	12,015	45,175	51,502	(12.3)
<i>% of Net Sales</i>	<i>31.0</i>	<i>37.9</i>		<i>30.8</i>	<i>29.0</i>	<i>30.1</i>	
Total Expenditure	33,251	34,719	(4.2)	32,873	126,566	130,012	(2.7)
<b>EBITDA</b>	<b>6,534</b>	<b>6,900</b>	<b>(5.3)</b>	<b>6,131</b>	<b>29,032</b>	<b>41,186</b>	<b>(29.5)</b>
<i>Margin (%)</i>	<i>16.4</i>	<i>16.6</i>		<i>15.7</i>	<i>18.7</i>	<i>24.1</i>	
Depreciation	2,728	2,674	2.0	2,804	10,859	9,122	19.0
<b>EBIT</b>	<b>3,806</b>	<b>4,225</b>	<b>(9.9)</b>	<b>3,327</b>	<b>18,173</b>	<b>32,064</b>	<b>(43.3)</b>
Other Income	2,003	1,368	46.4	1,037	3,947	4,810	(18.0)
Interest	585	406	44.1	540	2,044	1,525	34.0
Exceptional Items	(14,644)	-					
<b>PBT</b>	<b>(9,420)</b>	<b>5,187</b>	<b>(281.6)</b>	<b>3,824</b>	<b>20,076</b>	<b>35,349</b>	<b>(43.2)</b>
Extra-Ord. Inc./Exps.	47	18		(1)	36	(11)	
Total Taxes	(1,632)	1,367	(219.4)	1,608	2,885	9,785	(70.5)
<i>ETR (%)</i>	<i>17.3</i>	<i>26.4</i>		<i>42.0</i>	<i>14.4</i>	<i>27.7</i>	
<b>Reported PAT</b>	<b>(7,835)</b>	<b>3,802</b>	<b>(306.1)</b>	<b>2,217</b>	<b>17,156</b>	<b>25,575</b>	<b>(32.9)</b>

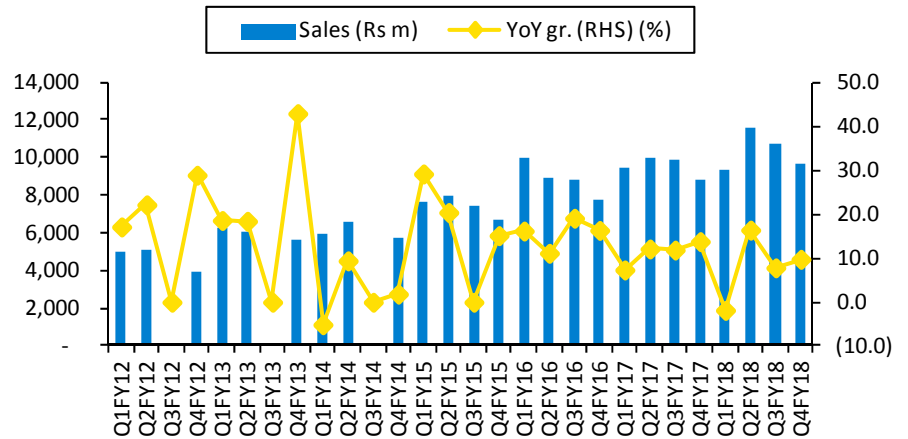
Source: Company Data, PL Research

**Exhibit 3: Major Sources of Revenues (Rs m)**

Y/e March	Q4FY18	Q4FY17	YoY gr. (%)	Q3FY18	FY18	FY17	YoY gr. (%)
Domestic market	9,647	8,788	9.8	10,688	41,253	38,157	8.1
<i>% of Sales</i>	24.2	21.1		27.4	26.5	22.3	
International market (Exports)	30,138	32,831	(8.2)	28,316	114,345	133,041	(14.1)
<i>% of Sales</i>	75.8	78.9		72.6	73.5	77.7	
<b>Total</b>	<b>39,785</b>	<b>41,619</b>	<b>(4.4)</b>	<b>39,004</b>	<b>155,598</b>	<b>171,198</b>	<b>(9.1)</b>
<b>Formulations</b>	<b>36,977</b>	<b>38,804</b>	<b>(4.7)</b>	<b>36,324</b>	<b>144,667</b>	<b>159,815</b>	<b>(9.5)</b>
<i>% of Sales</i>	92.9	93.2		93.1	93.0	93.4	
India	9,647	8,788	9.8	10,688	41,253	38,157	8.1
<i>% of Sales</i>	24.2	21.1		27.4	26.5	22.3	
<b>International market (Exports)</b>	<b>27,330</b>	<b>30,016</b>	<b>(8.9)</b>	<b>25,636</b>	<b>103,414</b>	<b>121,658</b>	<b>(15.0)</b>
<i>% of Sales</i>	68.7	72.1		65.7	66.5	71.1	
North America	14,990	19,007	(21.1)	14,321	58,939	82,627	(28.7)
<i>% of Sales</i>	37.7	45.7		36.7	37.9	48.3	
Europe, Middle East, Africa (EMEA)	3,513	3,012	16.6	2,721	11,252	10,115	
<i>% of Sales</i>	8.8	7.2		7.0	7.2	5.9	
Emerging Markets (ROW) & LATAM	2,190	1,879	16.6	1,852	7,498	6,261	19.8
<i>% of Sales</i>	5.5	4.5		4.7	4.8	3.7	
APAC	6,637	6,118	8.5	6,742	25,725	22,655	
<i>% of Sales</i>	16.7	14.7		17.3	16.5	13.2	
Non-Japan	1,583	2,075		1,207	25,725	7,003	
Japan	5,054	4,043	25.0	5,535	-	15,652	(100.0)
<i>% of Sales</i>	12.7	9.7		14.2	-	9.1	
<b>APIs</b>	<b>2,808</b>	<b>2,815</b>	<b>(0.2)</b>	<b>2,680</b>	<b>10,931</b>	<b>11,383</b>	<b>(4.0)</b>
<i>% of Sales</i>	7.1	6.8		6.9	7.0	6.6	
<b>Grand Total</b>	<b>39,785</b>	<b>41,619</b>	<b>(4.4)</b>	<b>39,004</b>	<b>155,598</b>	<b>171,198</b>	<b>(9.1)</b>

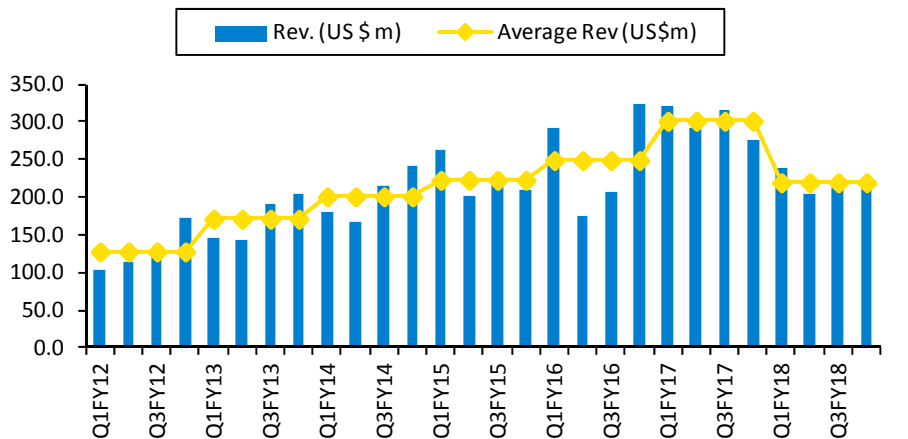
Source: Company Data, PL Research

**Exhibit 4: India formulation sales and growth: Acute makes pain in growth**



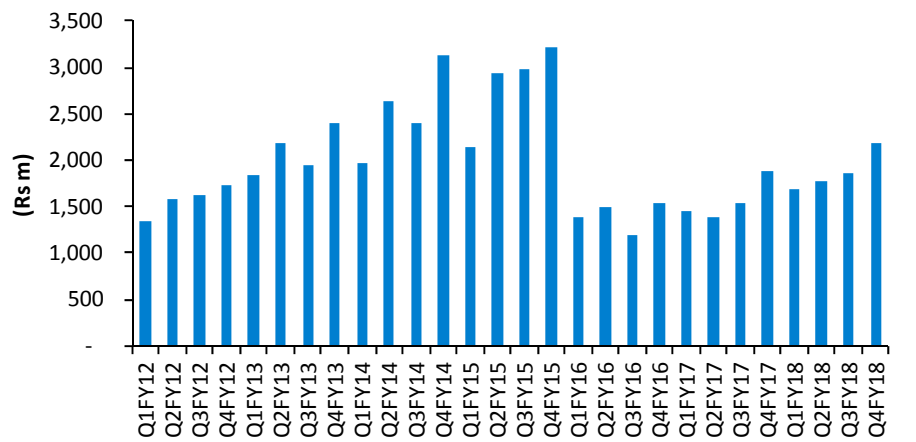
Source: Company Data, PL Research

**Exhibit 5: US generic sales (US\$ m): Current products facing strong pricing pressure**



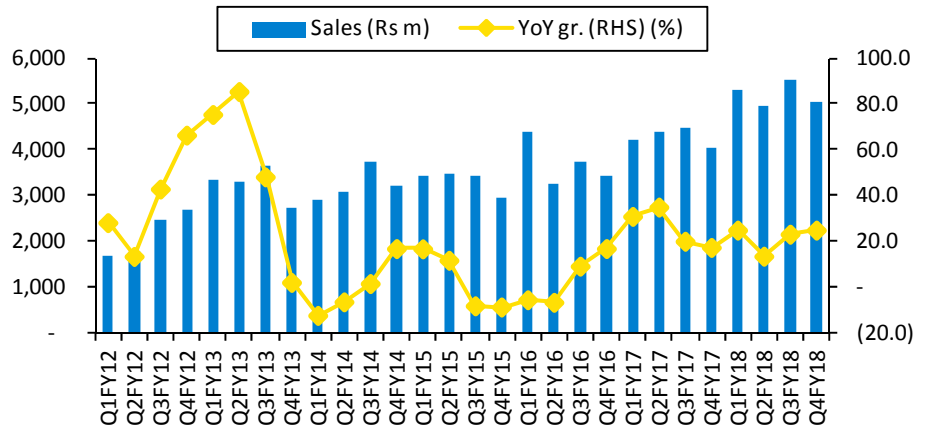
Source: Company Data, PL Research

**Exhibit 6: Emerging market sales: Acquisitions help in incorporating sales growth**



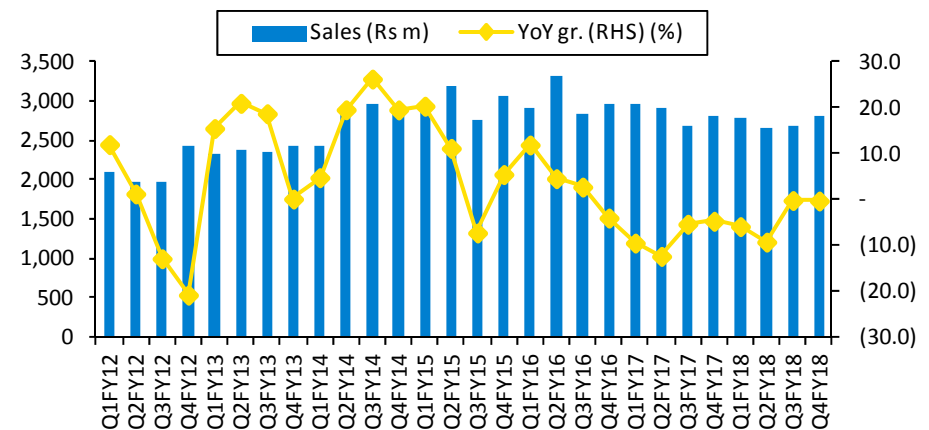
Source: Company Data, PL Research

**Exhibit 7: Japan generic sales, growth: Continue to be rickety on new price cut schedule**



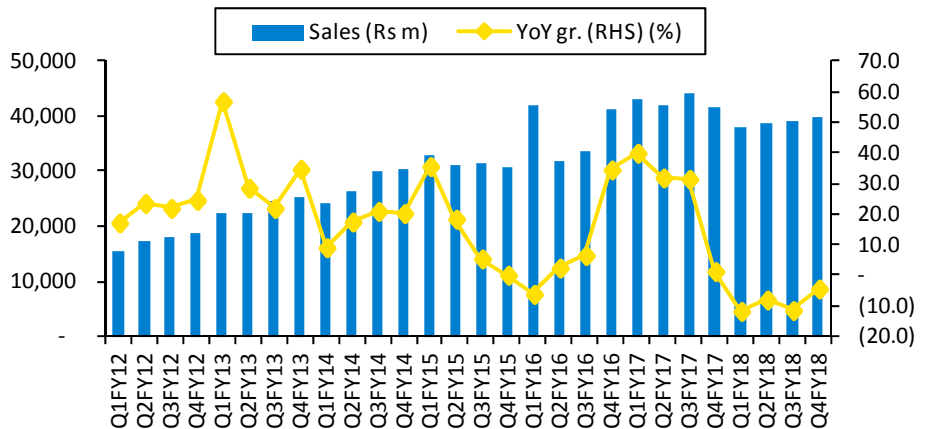
Source: Company Data, PL Research

**Exhibit 8: API sales and growth: Average performer**



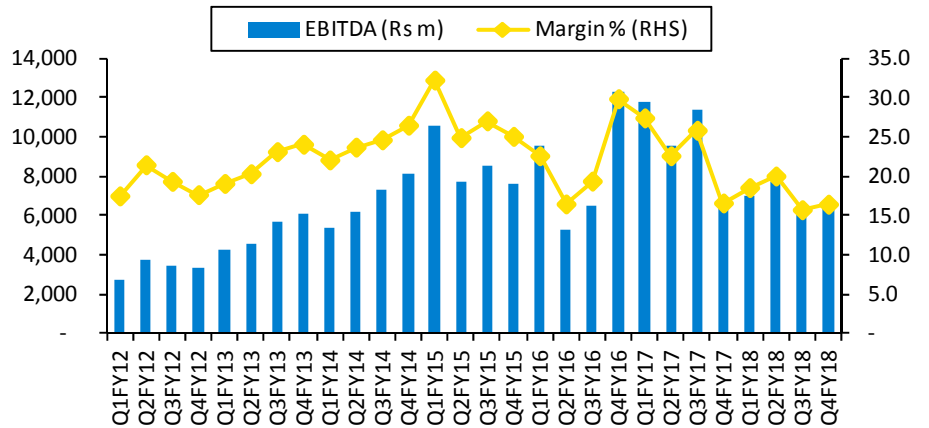
Source: Company Data, PL Research

**Exhibit 9: Sales, growth: Remain disappointing, no major headway in key geographies**



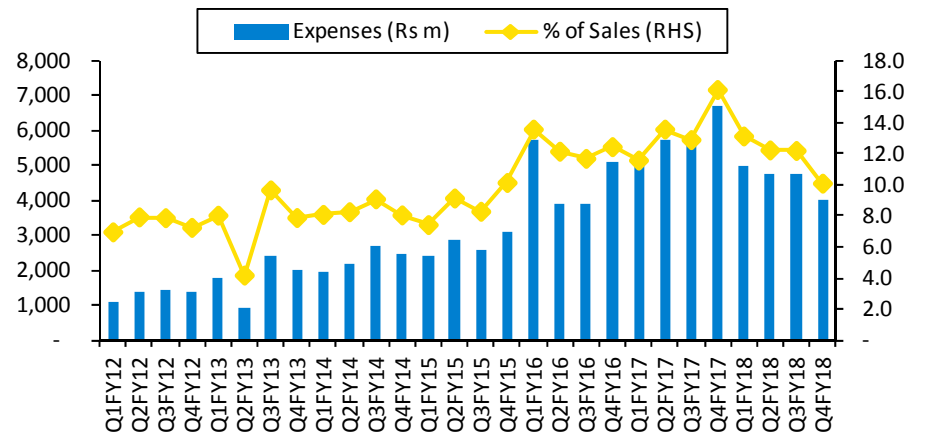
Source: Company Data, PL Research

**Exhibit 10: EBITDA and Margin: Strong price impact in top-5 US generics reduces margin**



Source: Company Data, PL Research

**Exhibit 11: R&D Exps as % of sales: Guided to be 12-13% in FY18E, FY19E**



Source: Company Data, PL Research

**Income Statement (Rs m)**

Y/e March	2017	2018	2019E	2020E
<b>Net Revenue</b>	<b>171,198</b>	<b>155,598</b>	<b>166,214</b>	<b>182,044</b>
Raw Material Expenses	50,014	52,744	55,682	62,805
Gross Profit	121,184	102,854	110,532	119,239
Employee Cost	28,495	28,647	29,918	30,037
Other Expenses	51,502	45,175	49,033	52,793
<b>EBITDA</b>	<b>41,186</b>	<b>29,032</b>	<b>31,581</b>	<b>36,409</b>
Depr. & Amortization	9,122	10,859	12,705	14,483
Net Interest	1,525	2,044	1,306	1,247
Other Income	4,810	3,947	4,026	4,106
<b>Profit before Tax</b>	<b>35,349</b>	<b>20,076</b>	<b>21,596</b>	<b>24,785</b>
Total Tax	9,785	2,885	6,047	6,940
<b>Profit after Tax</b>	<b>25,564</b>	<b>17,192</b>	<b>15,549</b>	<b>17,845</b>
Ex-Od items / Min. Int.	154	(29,181)	74	78
<b>Adj. PAT</b>	<b>25,575</b>	<b>17,156</b>	<b>15,474</b>	<b>17,767</b>
<b>Avg. Shares O/S (m)</b>	<b>451.6</b>	<b>452.1</b>	<b>452.1</b>	<b>452.1</b>
<b>EPS (Rs.)</b>	<b>56.6</b>	<b>37.9</b>	<b>34.2</b>	<b>39.3</b>

**Cash Flow Abstract (Rs m)**

Y/e March	2017	2018	2019E	2020E
C/F from Operations	41,148	(3,776)	20,277	20,682
C/F from Investing	(25,287)	11,541	(17,011)	(17,085)
C/F from Financing	4,332	(12,941)	(10,717)	(3,930)
Inc. / Dec. in Cash	20,193	(5,175)	(7,451)	(333)
Opening Cash	7,802	28,135	22,960	15,509
Closing Cash	27,995	22,960	15,509	15,176
FCFF	7,988	19,405	14,292	15,043
FCFE	15,873	8,507	4,881	12,360

**Key Financial Metrics**

Y/e March	2017	2018	2019E	2020E
<b>Growth</b>				
Revenue (%)	24.4	(9.1)	6.8	9.5
EBITDA (%)	29.2	(29.5)	8.8	15.3
PAT (%)	13.1	(32.9)	(9.8)	14.8
EPS (%)	12.9	(33.0)	(9.8)	14.8
<b>Profitability</b>				
EBITDA Margin (%)	24.1	18.7	19.0	20.0
PAT Margin (%)	14.9	11.0	9.3	9.8
RoCE (%)	12.9	8.5	7.7	8.7
RoE (%)	20.7	12.7	11.1	11.8
<b>Balance Sheet</b>				
Net Debt : Equity	0.4	0.4	0.3	0.3
Net Wrkng Cap. (days)	169	147	134	124
<b>Valuation</b>				
PER (x)	13.3	19.8	21.9	19.1
P / B (x)	2.5	2.5	2.4	2.2
EV / EBITDA (x)	9.5	13.5	12.1	10.4
EV / Sales (x)	2.3	2.5	2.3	2.1
<b>Earnings Quality</b>				
Eff. Tax Rate	27.7	14.4	28.0	28.0
Other Inc / PBT	13.6	19.7	18.6	16.6
Eff. Depr. Rate (%)	9.0	10.5	10.7	10.8
FCFE / PAT	62.1	49.6	31.5	69.6

Source: Company Data, PL Research.

**Balance Sheet Abstract (Rs m)**

Y/e March	2017	2018	2019E	2020E
Shareholder's Funds	134,976	135,771	143,085	156,782
Total Debt	79,661	68,763	59,352	56,669
Other Liabilities	13,413	12,083	11,555	7,483
<b>Total Liabilities</b>	<b>228,050</b>	<b>216,616</b>	<b>213,992</b>	<b>220,933</b>
Net Fixed Assets	108,560	105,117	110,011	113,385
Goodwill	23,100	24,485	24,975	26,223
Investments	985	927	968	1,307
Net Current Assets	81,519	75,658	75,386	76,467
<i>Cash &amp; Equivalents</i>	<i>28,135</i>	<i>16,429</i>	<i>17,270</i>	<i>16,145</i>
<i>Other Current Assets</i>	<i>91,406</i>	<i>105,667</i>	<i>102,880</i>	<i>104,884</i>
<i>Current Liabilities</i>	<i>38,023</i>	<i>46,438</i>	<i>44,764</i>	<i>44,561</i>
Other Assets	13,886	10,430	2,654	3,551
<b>Total Assets</b>	<b>228,050</b>	<b>216,616</b>	<b>213,992</b>	<b>220,933</b>

**Quarterly Financials (Rs m)**

Y/e March	Q1FY18	Q2FY18	Q3FY18	Q4FY18
<b>Net Revenue</b>	<b>38,068</b>	<b>38,742</b>	<b>39,004</b>	<b>39,785</b>
<b>EBITDA</b>	<b>7,056</b>	<b>7,753</b>	<b>6,131</b>	<b>6,534</b>
<i>% of revenue</i>	<i>18.5</i>	<i>20.0</i>	<i>15.7</i>	<i>16.4</i>
Depr. & Amortization	2,605	2,722	2,804	2,728
Net Interest	439	479	540	585
Other Income	947	1,518	1,037	2,003
<b>Profit before Tax</b>	<b>4,959</b>	<b>6,070</b>	<b>3,824</b>	<b>5,223</b>
Total Tax	1,368	1,541	1,608	(1,632)
<b>Profit after Tax</b>	<b>3,581</b>	<b>4,550</b>	<b>2,217</b>	<b>6,808</b>
<b>Adj. PAT</b>	<b>3,581</b>	<b>4,550</b>	<b>2,217</b>	<b>(7,835)</b>

**Key Operating Metrics (Rs m)**

Y/e March	2017	2018	2019E	2020E
India Formulations	38,157	41,253	46,203	51,286
North America	92,742	70,191	73,513	79,964
APAC	15,652	20,645	23,458	27,364
ROW Formulations & LATAM	13,264	12,578	13,468	14,470
APIs	11,383	10,931	10,542	10,038
Total	171,198	155,598	167,184	183,121

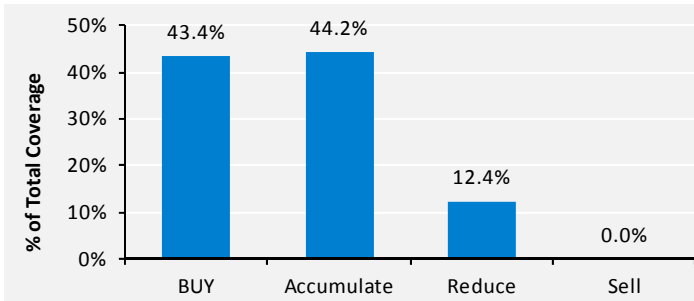
Source: Company Data, PL Research.



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**Rating Distribution of Research Coverage**



**PL's Recommendation Nomenclature**

<b>BUY</b>	: Over 15% Outperformance to Sensex over 12-months
<b>Accumulate</b>	: Outperformance to Sensex over 12-months
<b>Reduce</b>	: Underperformance to Sensex over 12-months
<b>Sell</b>	: Over 15% underperformance to Sensex over 12-months
<b>Trading Buy</b>	: Over 10% absolute upside in 1-month
<b>Trading Sell</b>	: Over 10% absolute decline in 1-month
<b>Not Rated (NR)</b>	: No specific call on the stock
<b>Under Review (UR)</b>	: Rating likely to change shortly

**DISCLAIMER/DISCLOSURES**

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