

INDUSTRY PHARMA
CMP (as on 09 Feb 2017) Rs 1,490
Target Price Rs 2,080

Nifty	8,778
Sensex	28,330

KEY STOCK DATA

Bloomberg	LPC IN
No. of Shares (mn)	451
MCap (Rs bn) / (\$ mn)	673/10,050
6m avg traded value (Rs mn)	1,635

STOCK PERFORMANCE (%)

52 Week high / low	Rs 1,912/1,280		
	3M	6M	12M
Absolute (%)	(2.5)	(7.2)	(21.7)
Relative (%)	(6.5)	(8.1)	(39.7)

SHAREHOLDING PATTERN (%)

Promoters	46.7
FIs & Local MFs	8.2
FIIIs	33.3
Public & Others	11.8

Source : BSE
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Good show

Lower than expected R&D costs (12.9% of sales vs. 14% expected) led to a surprise beat in margins (27.1%) in 3QFY17. Boosted by this, earnings grew ~20%YoY to Rs 6.3bn, despite higher taxes during this quarter. Revenue performance continued to be strong and in line with estimates, growing at ~26% to Rs ~45bn. US sales grew ~58% YoY, and notably, ~9% sequentially on a high base. With (1) continued semi exclusivity in gGlumetza and gFortamet, (2) scale up in Gavis portfolio, (3) new product launches in 4QFY17/1QFY18 and (4) a quality pipeline of 150+ ANDAs, LPC is well placed for the near and long term. On higher bases, we foresee ~17% rev. CAGR and ~22% earnings CAGR over FY17-19E. At CMP, the stock trades at 18.6x FY18E and 15.0x FY19E, a 20-25% discount to the historical average. With the expected launches of exclusive/low competition products and attractive valuations, **re-iterate BUY with a TP of Rs 2,080 (22x on Dec-18E).**

- LPC continued its investment in complex generic products during the quarter, and the pipeline looks impressive. With products from injectables, respiratory

and biosimilar categories being filed, near term launches of gMinastrin (under 180 day exclusivity), gEpzicom, Hydrocodon and a scale up in existing products like Methergine, the future looks bright for LPC. We expect approvals from the US FDA to pick up and LPC to launch 50+ products in the US market over FY18-19E, including exclusive products like – gFosrenol, gRenvela, gWelchol, gRenagel, gTamiflu and gTruvada.

Highlight of the quarter

- **Concall takeaways:** (1) Competition in gGlumetza expected in 2QCY18 at the earliest, Valeant's AG launch not to be significant, (2) Impact of Mylan's entry in gFortamet is growing, (3) Methergine sales in 3QFY17 were ~US\$ 12mn, total branded sales ~US\$22 mn (4) LPC to file ~30 ANDAs and launch 25+ products in FY18, (5) Albuterol MDI filed in the US in 3Q, gAdvair clinical trials to begin soon with filing expected in FY18, (6) India business expected to grow at ~15% over the next 2 years, (7) Full impact of Shinogi acquisition will be visible in 4Q, (8) Tax rate to be ~28% for FY17.
- **Near term outlook:** Pick up in ANDA approvals to drive share price.

Financial Summary

(Rsmn)	3QFY17	3QFY16	YoY (%)	2QFY17	QoQ (%)	FY16	FY17E	FY18E	FY19E
Net Sales	44,829	35,558	26.1	42,905	4.5	142,085	180,097	209,901	245,872
EBIDTA	12,158	8,772	38.6	10,741	13.2	37,534	49,527	58,143	70,074
APAT	6,331	5,298	19.5	6,622	(4.4)	22,706	30,237	36,157	44,845
Diluted adj. EPS (Rs)	14.0	11.7	19.5	14.7	(4.4)	50.4	67.0	80.1	99.3
P/E (x)						29.6	22.2	18.6	15.0
RoE (%)						22.9	24.7	23.9	24.0

Source: Company, HDFC sec Inst Research # Consolidated

The US business was the main growth driver for LPC in 3QFY17

YoY jump in employee cost is on account of inorganic expansion

Other income contains significant amount of forex gains which were not present in the previous quarter (forex loss in 2Q)

Tax was higher during the quarter due to unwinding of deferred tax asset

EBITDA margins surprised positively, beating estimates by 180bps. This was largely on account of the lower than expected R&D spend

Quarterly Financials Snapshot (Consolidated)

Particulars	3QFY17	3QFY16	YoY (%)	2QFY17	QoQ (%)	3QFY17E	Var (%)
Net Sales	44,829	35,558	26.1	42,905	4.5	43,686	2.6
Material Expenses	13,016	11,230	15.9	12,429	4.7	12,831	1.4
Employee Expenses	7,312	5,284	38.4	7,124	2.6	6,968	4.9
R&D Expenses	5,682	3,916	45.1	5,716	(0.6)	5,948	(4.5)
Other Expenses	6,661	6,357	4.8	6,896	(3.4)	6,883	(3.2)
EBITDA	12,158	8,772	38.6	10,741	13.2	11,057	10.0
Depreciation	2,309	1,114		2,112		2,200	
EBIT	9,849	7,658	28.6	8,629	14.1	8,857	11.2
Other Income	295.80	653		271		520	
Interest cost	459	92		263		290	
Forex gain/(loss)	740			(460)			
PBT	10,426	8,219	26.8	8,177	27.5	9,087	14.7
Tax	4,095	2,909		1,589		2,850	
RPAT	6,331	5,310	19.2	6,588	(3.9)	6,237	1.5
Minority interest + Share of Asso.	0	(13)		(34)		(65)	
APAT	6,331	5,298	19.5	6,622	(4.4)	6,172	2.6

Source: Company, HDFC sec Inst Research

Margin Analysis

	3QFY17	3QFY16	YoY (bps)	2QFY17	QoQ (bps)	3QFY17E	Var (bps)
Material Expenses % Net Sales	29.0	31.6	(255)	29.0	7	29.4	(34)
Employee Expenses % Net Sales	16.3	14.9	145	16.6	(29)	15.9	36
R&D Expenses % Net Sales	12.7	11.0	166	13.3	(65)	13.6	(94)
Other Expenses % Net Sales	14.9	17.9	(302)	16.1	(121)	15.8	(90)
EBITDA Margin (%)	27.1	24.7	245	25.0	209	25.3	181
Tax Rate (%)	39.3	35.4	388	19.4	1,984	31.4	791
APAT Margin (%)	14.1	14.9	(78)	15.4	(131)	14.1	(0)

Source: Company, HDFC sec Inst Research

US branded sales are scaling up on the back of increased revenues from Methergine.

Pricing pressure on the base business continues to be in high single digit. Growth YoY continues to be significant on the back of windfall sales from gGlumetza and gFortamet

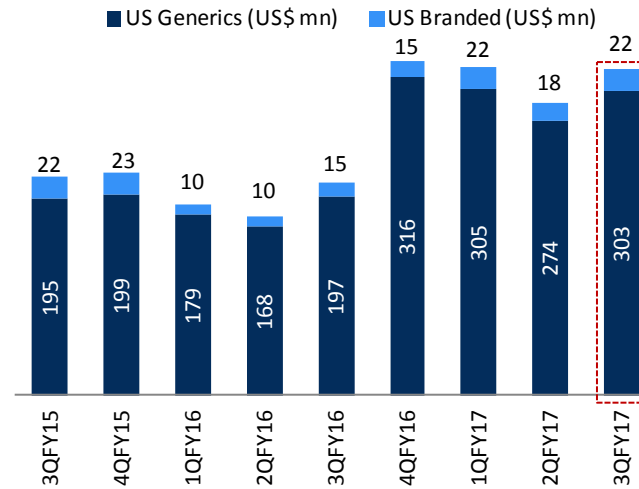
On a higher base, we foresee US rev. growth of 17% CAGR over FY17-19E

India revenues grew ~12% despite various headwinds in the domestic market

We foresee EBITDA growth of ~19% over FY17-19E, with margins settling at ~28.5% by FY19E

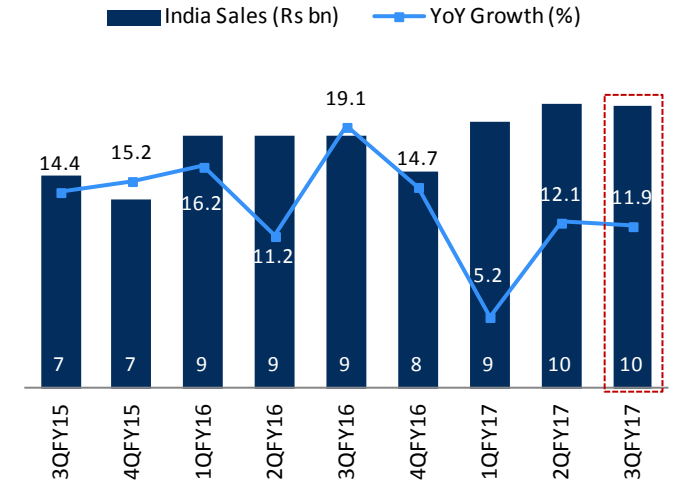
R&D expense was at 12.9% of sales for 3QFY17, below expected levels. It is likely to be in the 13-14% range going forward

US Formulations - Trend



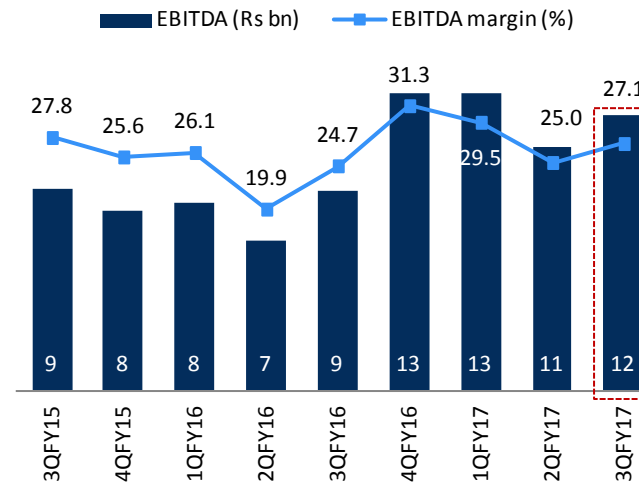
Source: Company, HDFC sec Inst Research

India-branded Formulation Growth Trajectory



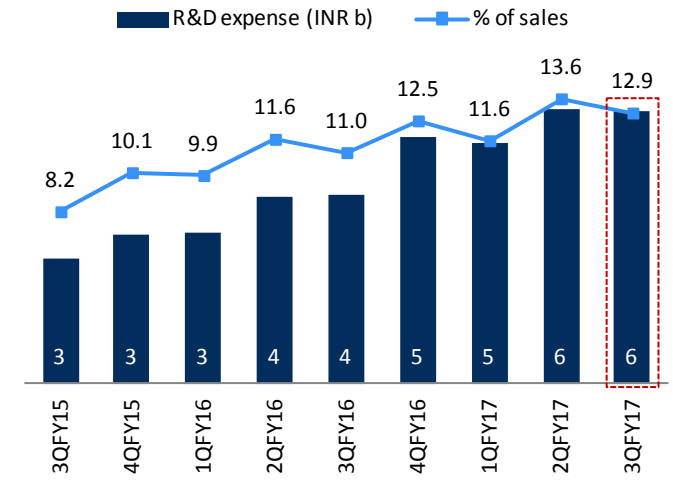
Source: Company, HDFC sec Inst Research

EBITDA Margin Trajectory



Source: Company, HDFC sec Inst Research

R&D expense as % of sales



Source: Company, HDFC sec Inst Research

US business grew ~58%YoY (rupee terms) led by gGlumetza and gFortamet in 3QFY17, beating estimates Sequential growth was also positive at ~9%

India business recorded strong growth of ~12% despite impact of demonetization and other headwinds

APAC revenues were below estimates mainly on account of a temporary blip in Japan caused by a change in government policies towards pharmacies for selling generic drugs

The US and India businesses are likely to drive top-line over FY17-19E

We also expect strong growth from Japan segment upon full realization of recently acquired Shionogi portfolio

Segmental Quarterly Performance

(Rs mn)	3QFY17	3QFY16	YoY (%)	2QFY17	QoQ (%)	3QFY17E	Var (%)
India	9,912	8,860	11.9	9,958	(0.5)	10,036	(1.2)
US	21,755	13,805	57.6	19,978	8.9	19,314	12.6
APAC	5,601	4,634	20.9	5,520	1.5	6,010	(6.8)
EMEA	2,555	2,187	16.8	2,355	8.5	2,492	2.5
RoW	1,175	885	32.8	986	19.2	1,130	4.0
LATAM	367	297	23.6	396	(7.3)	400	(8.3)
API & others	2,684	2,835	(5.3)	2,919	(8.1)	3,073	(12.6)
Total	44,049	33,503	31.5	42,112	4.6	42,455	3.8

Source: HDFC sec Inst Research

Assumptions

	FY16	FY17E	FY18E	FY19E
India	33,916	39,003	45,829	53,849
Growth (%)	14.3	15.0	17.5	17.5
US	59,407	85,739	97,104	116,766
Growth (%)	5.0	44.3	13.3	20.2
APAC	17,619	24,208	29,910	33,640
Growth (%)	3.1	44.9	25.1	11.6
EMEA	8,634	9,968	11,853	13,512
Growth (%)	30.5	29.4	12.8	11.6
LATAM	3,841	4,372	5,152	6,011
Growth (%)	-	13.8	17.8	16.7
RoW	1,281	1,532	1,726	1,926
Growth (%)	-	19.6	12.6	11.6
API & Others	12,074	11,248	12,454	13,646
Growth (%)	1.1	(6.8)	10.7	9.6
Total	136,772	176,070	204,029	239,350
Growth (%)	8.7	28.9	15.7	17.4

Source: HDFC sec Inst Research

Income Statement (Consolidated)

Year ending March (Rs mn)	FY15	FY16	FY17E	FY18E	FY19E
Net Revenues	1,27,700	1,42,085	180,097	209,901	245,872
Growth (%)	13.1	11.3	26.8	16.5	17.1
Material Expenses	41,570	43,094	52,769	61,291	70,074
Employee Expenses	17,473	21,077	28,455	30,436	33,684
SG&A Expenses	6,946	11,935	11,706	14,903	18,686
Other Expenses	25,515	28,444	37,640	45,129	53,354
EBITDA	36,196	37,534	49,527	58,143	70,074
EBITDA Margin (%)	28.3	26.4	27.5	27.7	28.5
EBITDA Growth (%)	20.5	3.7	32.0	17.4	20.5
Depreciation	4,347	4,635	8,788	10,227	10,816
EBIT	31,849	32,899	40,739	47,915	59,258
Other Income (Incl EO Items)	2,398	1,877	2,250	3,000	3,500
Interest	98	447	1,295	1,042	915
PBT	34,148	34,329	41,694	49,873	61,843
Tax (Incl Deferred)	9,704	11,536	11,258	13,466	16,698
RPAT	24,444	22,794	30,437	36,407	45,145
EO (Loss) / Profit (Net Of Tax)	412	88	200	250	300
APAT	24,032	22,706	30,237	36,157	44,845
APAT Growth (%)	30.9	(5.5)	33.2	19.6	24.0
Adjusted EPS (Rs)	53.5	50.4	67.0	80.1	99.3

Source: Company, HDFC sec Inst Research

Balance Sheet (Consolidated)

Year ending March (Rs mn)	FY15	FY16	FY17E	FY18E	FY19E
SOURCES OF FUNDS					
Share Capital - Equity	899	901	903	903	903
Reserves	87,842	1,08,943	134,426	165,829	205,921
Total Shareholders' Funds	88,741	1,09,844	135,329	166,732	206,824
Minority Interest	241	321	521	771	771
Long-term Debt	1,018	53,739	53,119	48,119	43,119
Short-term Debt	3,692	17,454	11,954	9,454	6,954
Total Debt	4,710	71,193	65,073	57,573	50,073
Net Deferred Taxes	1,182	1,239	1,239	1,239	1,239
Long-term Provisions & Others	2,496	3,651	3,651	3,651	3,651
TOTAL SOURCES OF FUNDS	97,370	1,86,247	205,812	229,966	262,557
APPLICATION OF FUNDS					
Net Block	26,636	59,379	78,336	81,309	83,693
CWIP	6,745	32,122	27,300	25,600	25,600
Intangible assets	17,046	29,644	29,644	29,644	29,644
Investments	16,584	75	150	225	225
LT Loans & Advances	1,760	4,581	4,750	4,750	4,750
Total Non-current Assets	68,771	1,25,801	140,180	141,528	143,912
Inventories	25,036	31,787	34,300	38,613	44,146
Debtors	26,566	45,498	43,196	46,146	54,054
Other Current Assets	5,350	12,106	10,349	11,410	12,302
Cash & Equivalents	4,814	8,379	12,815	32,229	53,292
Total Current Assets	61,765	97,770	100,659	128,398	163,794
Creditors	19,561	21,919	21,107	24,516	28,029
Other Current Liabilities & Provisions	13,605	15,406	13,920	15,443	17,120
Total Current Liabilities	33,166	37,324	35,027	39,960	45,149
Net Current Assets	28,599	60,446	65,632	88,438	118,645
TOTAL APPLICATION OF FUNDS	97,370	1,86,247	205,812	229,966	262,557

Source: Company, HDFC sec Inst Research

Cash Flow

Year ending March (Rs mn)	FY15	FY16	FY17E	FY18E	FY19E
Reported PBT	34,148	34,329	41,694	49,873	61,843
Non-operating & EO items	(129)	(36)	(2,561)	(3,576)	(3,576)
Interest expenses	98	447	1,295	1,042	915
Depreciation	4,347	4,635	8,788	10,227	10,816
Working Capital Change	7,364	(34,084)	(797)	(3,392)	(9,144)
Tax Paid	(10,300)	(11,479)	(11,258)	(13,466)	(16,698)
OPERATING CASH FLOW (a)	35,528	(6,188)	37,161	40,709	44,156
Capex	(16,726)	(70,670)	(23,045)	(11,500)	(13,200)
Free cash flow (FCF)	18,802	(76,858)	14,116	29,209	30,956
Investments	(14,799)	16,509	(75)	(75)	-
Non-operating Income	131	189	2,561	3,576	3,276
INVESTING CASH FLOW (b)	(31,395)	(53,972)	(20,558)	(7,999)	(9,924)
Debt Issuance/(Repaid)	(1,282)	66,483	(6,120)	(7,500)	(7,500)
Interest Expenses	(98)	(447)	(1,295)	(1,042)	(915)
FCFE	2,753	5,876	9,188	24,167	25,817
Share Capital Issuance	(1,766)	2,343	2	0	0
Dividend	(3,681)	(3,954)	(4,754)	(4,754)	(4,754)
FINANCING CASH FLOW (c)	(6,828)	64,425	(12,166)	(13,296)	(13,169)
NET CASH FLOW (a+b+c)	(2,694)	4,265	4,436	19,414	21,064
EO Items, Others	(467)	(700)	-	-	-
Closing Cash & Equivalents	(3,161)	3,565	4,436	19,414	21,064

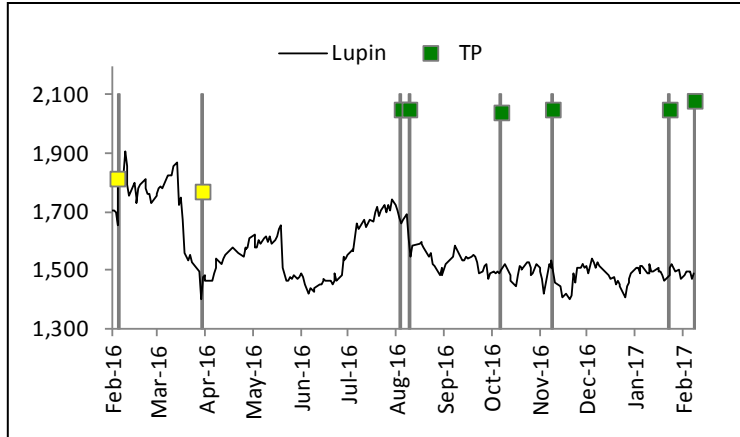
Source: Company, HDFC sec Inst Research

Key Ratios

	FY15	FY16	FY17E	FY18E	FY19E
PROFITABILITY (%)					
GPM	67.4	69.7	70.7	70.8	71.5
EBITDA Margin	28.3	26.4	27.5	27.7	28.5
APAT Margin	18.8	16.0	16.8	17.2	18.2
RoE	30.4	22.9	24.7	23.9	24.0
RoIC (or Core RoCE)	30.7	12.6	16.5	18.4	21.8
RoCE	27.2	16.2	16.8	18.9	22.4
EFFICIENCY					
Tax Rate (%)	28.4	33.6	27.0	27.0	27.0
Fixed Asset Turnover (x)	2.8	2.5	2.5	2.5	2.6
Inventory (days)	71.6	81.7	69.5	67.1	65.5
Debtors (days)	75.9	116.9	87.5	80.2	80.2
Other Current Assets (days)	15.3	31.1	21.0	19.8	18.3
Payables (days)	55.9	56.3	42.8	42.6	41.6
Other Current Liab & Provns (days)	38.9	39.6	28.2	26.9	25.4
Cash Conversion Cycle (days)	68.0	133.8	107.0	97.7	97.0
Debt/EBITDA (x)	0.1	1.9	1.3	1.0	0.7
Net D/E (x)	(0.0)	0.6	0.4	0.2	(0.0)
Interest Coverage (x)	324.7	73.6	31.5	46.0	64.8
PER SHARE DATA (Rs)					
EPS	53.5	50.4	67.0	80.1	99.3
Dividend	7.0	7.5	9.0	9.0	9.0
Book Value	197.4	243.8	299.8	369.3	458.1
VALUATION					
P/E (x)	29.1	30.9	22.2	18.6	15.0
P/BV (x)	7.9	6.4	5.0	4.0	3.3
EV/EBITDA (x)	19.3	20.3	14.6	12.0	9.6
EV/Revenues (x)	5.5	5.4	4.0	3.3	2.7
OCF/EV (%)	5.1	(0.8)	5.1	5.8	6.6
FCF/EV (%)	2.7	(10.1)	1.9	4.2	4.6
FCFE/Mkt Cap (%)	0.4	0.8	1.4	3.6	3.9
Dividend Yield (%)	0.5	0.5	0.6	0.6	0.6

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
8-Feb-16	1,803	NEU	1,810
30-Mar-16	1,475	NEU	1,767
4-Aug-16	1,658	BUY	2,050
10-Aug-16	1,607	BUY	2,050
8-Oct-16	1,498	BUY	2,040
10-Nov-16	1,530	BUY	2,050
23-Jan-17	1,479	BUY	2,050
10-Feb-17	1,490	BUY	2,080

Rating Definitions

- BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
- NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
- SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

Disclosure:

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