

### FY18 outlook in line with our estimates

## Quick Note

Fig. 1: LPC: 4QFY17 results synopsis

<b>Above or below</b>	Revenue/EBITDA came in ~6%/34% lower than our estimates. However, EBITDA adjusted for one-offs was ~7% lower than our forecast.
<b>What to make of it</b>	Lower-than-expected revenue in the US resulted in overall revenue miss. Lower US sales were on account of drop in gGlumetza/gFortamet sales and lower channel filling for gMinastrin 24Fe in our view. The company booked one-off expense of ~INR3.2bn (INR1.7bn due to forex losses and INR1.6bn on account of provisioning for litigation loss in Australia) during 4Q17, this impacted EBITDA margin by ~8%. Higher R&D expense (~16% of sales) also was a drag on margins.
<b>Key numbers</b>	Revenues came in at INR42.5bn (+1.3% y-y). US sales at USD276mn down USD40mn q-q. India sales at INR8.8bn (+13.8% y-y). Japan sales at INR4.7bn (+35.7% y-y). EBITDA adjusted for one-offs at INR11.0bn (-16% y-y). Adjusted EBITDA margin at ~26%.
<b>What next</b>	US sales growth during FY18 expected to be muted on account of pricing pressure in the base business and decline in gGlumetza/gFortamet sales. Management expects FY18 EBITDA margin at 26-28%. New launches will remain key for countering the US sales drop.

Source: Company data, Nomura estimates

4QFY17 results came in below our estimates due to lower US revenues and certain one-time expenses. US revenues fell USD 40m Q-Q on lower gMinastrin 24Fe and higher erosion in gGlumetza. EBITDA at INR7.8bn vs our estimate of INR11.9bn. One-time expenses and forex loss accounted for INR3.2bn of the miss. R&D spend at INR6.7bn was INR700mn ahead of our estimate. Adjusted for the one-time charge, higher R&D spend and forex loss, we think EBITDA was ~2% lower vs our estimate. Relatively strong growth in India and other EMs were positives. As expected, management guided towards flattish US sales growth in FY18F due to limited high value launches and erosion in the base business. Management expects R&D spend to remain flat in FY18F and guided towards 26-28% EBITDA margin, in line with our expectation. Capex intensity is also expected to come down in FY18. We like the company's attempt to move up the value chain. The complex generic portfolio is making progress with inhalation filings, near-term commencement of biostudies of long-acting injectables and potential first biosimilar filing in EU in FY18F.

Lupin is trading at 20.6x and 15.6x on our FY18/19F EPS estimates of INR59.5/78.5. We attribute 19x March 2019F EPS to arrive at our target price of INR1,491. We retain our Buy rating.

Key risks: 1) delay in approval of key products; 2) adverse currency movement; and 3) adverse regulatory developments.

### Global Markets Research

25 May 2017

<b>Rating</b> Remains	<b>Buy</b>
<b>Target Price</b> Remains	INR 1491
<b>Closing price</b> 24 May 2017	INR 1228

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Fig. 2: Quarterly revenue breakup

INRm

	4QFY16	3QFY17	4QFY17	% Chg (Y-Y)	% Chg (Q-Q)	4QFY17 Nom ests	vs Nom ests (%)
<b>Formulations</b>	<b>38,137</b>	<b>41,365</b>	<b>38,804</b>	<b>1.7%</b>	<b>-6.2%</b>	<b>41,727</b>	<b>-7.0%</b>
US	21,901	21,755	19,007	-13.2%	-12.6%	22,934	-17.1%
India	7,722	9,912	8,788	13.8%	-11.3%	8,241	6.6%
Japan	3,449	4,470	4,680	35.7%	4.7%	5,174	-9.6%
RoW (incl South Africa)	3,748	3,788	4,962	32.4%	31.0%	4,012	23.7%
Europe & Middle East	1,317	1,440	1,368	3.8%	-5.0%	1,366	0.1%
<b>API</b>	<b>2,953</b>	<b>2,684</b>	<b>2,815</b>	<b>-4.7%</b>	<b>4.9%</b>	<b>2,750</b>	<b>2.4%</b>
<b>Total Sales</b>	<b>41,090</b>	<b>44,049</b>	<b>41,619</b>	<b>1.3%</b>	<b>-5.5%</b>	<b>44,477</b>	<b>-6.4%</b>

Source: Company data, Nomura estimates

Fig. 3: Quarterly P&amp;L

INRm

	4QFY16	3QFY17	4QFY17	% Chg (Y-Y)	% Chg (Q-Q)	4QFY17 Nom ests	vs Nom ests (%)
Net Sales	41,090	44,049	41,619	1.3%	-5.5%	44,477	-6.4%
Other Operating Income	884	779	914	3.4%	17.3%	900	1.6%
<b>Total Revenue</b>	<b>41,974</b>	<b>44,829</b>	<b>42,533</b>	<b>1.3%</b>	<b>-5.1%</b>	<b>45,377</b>	<b>-6.3%</b>
Material Cost	11,010	13,016	11,851	7.6%	-8.9%	13,125	-9.7%
Staff Cost	5,681	7,312	7,078	24.6%	-3.2%	7,644	-7.4%
Other Expense	12,135	12,343	15,791	30.1%	27.9%	12,696	24.4%
<b>EBITDA</b>	<b>13,149</b>	<b>12,158</b>	<b>7,814</b>	<b>-40.6%</b>	<b>-35.7%</b>	<b>11,913</b>	<b>-34.4%</b>
Other Income	349	1,036	453	30.0%	-56.2%	943	-51.9%
Interest Expense	310	459	406	31.0%	-11.6%	479	-15.3%
Depreciation	1,488	2,309	2,674	79.7%	15.8%	2,395	11.7%
<b>PBT</b>	<b>11,700</b>	<b>10,426</b>	<b>5,187</b>	<b>-55.7%</b>	<b>-50.3%</b>	<b>9,981</b>	<b>-48.0%</b>
Tax	4,188	4,095	1,367	-67.4%	-66.6%	3,050	-55.2%
<b>Net Profit</b>	<b>7,512</b>	<b>6,331</b>	<b>3,820</b>	<b>-49.2%</b>	<b>-39.7%</b>	<b>6,932</b>	<b>-44.9%</b>
Minority interest	51	24	34			-	
Share of Profit from JVs	19	24	16			-	
<b>Net profit after MI</b>	<b>7,480</b>	<b>6,331</b>	<b>3,802</b>	<b>-49.2%</b>	<b>-39.9%</b>	<b>6,932</b>	<b>-45.2%</b>
				<b>bps Chg (Y-Y)</b>	<b>bps Chg (Q-Q)</b>		<b>vs Nom ests</b>
Gross margin (%)	73.2%	70.5%	71.5%	(168)	107	70.5%	103
EBITDA margin (%)	31.3%	27.1%	18.4%	(1,295)	(875)	26.3%	(788)
Tax rate (%)	35.8%	39.3%	26.4%	(944)	(1,292)	30.6%	(420)

Source: Company data, Nomura estimates

## Conference call takeaways

### North America: No big launch in FY18F+ Pricing pressure and additional competition = Flat US in FY18F vs FY17

- US sales at USD276mn during the quarter declined USD40m q-q. US branded sales at USD22m declined ~USD6m q-q. We think the remaining drop q-q was primarily on account of lower contribution from key products such as gGlumetza and gFortamet.
- FY17 US branded sales at USD78m were up 90% y-y. Methergine sales are ramping up slowly and the company expects the product to achieve peak sales of USD 60mn.
- Lupin received 34 ANDA approvals and launched 18 products during FY17. 11 products were commercialized in 4Q17. Management expects 30+ launches in FY18/19F in the US going forward.
- Pricing pressure in the base business during FY17 ex gGlumetza/gFortamet was in single digits as per company management. Pricing pressure to remain as Express Script joins the Walgreen consortium for generic sourcing going forward.

- Lupin filed 37 ANDAs during FY17, taking the cumulative pending ANDAs to 154 (market size USD76bn). The company currently has 28 First to Files (FTF) pending approval (market size USD12.4bn); of these it has sole exclusivity in 11, as per management.
- In gRenvela/Renagel, the company is in the process of submitting its response to the complete response letter (CRL) issued by the FDA. Management expects to submit the response by FY18F-end and gain approval by FY19F-end as of now.
- **In FY18F, management expects flattish sales in the US, in line with our expectations.**

#### India

- Management expects to record to sustain above average market growth.

#### Japan: Market getting tougher with annual price reductions

- During FY17, the company bulked up its CNS portfolio by acquiring 21 brands from Shionogi and Quetiapine fumarate Tabs XR from Astellas.
- In Japan, the government is considering generic price cuts on annual basis vs bi-annual earlier. Clarity on this is expected by Oct 2017.

#### Margins: Expect to hold on despite pricing challenges

- Management expects EBITDA margin at 26-28% in FY18F compared to 26.3% in FY17.

#### R&D: No significant rise from FY17 levels

- R&D spend during 4Q17 was at INR6.7bn (~16.1% of sales). FY17 R&D spend at INR23.1bn was at ~13% of sales. Management expects R&D spend to remain flat Y-Y.
- ~35% of the FY17 R&D spend are on specialty, inhalation, biosimilars that are not contributing to revenues currently.
- Inhalation: The company filed gProair MDI in Jan 2017. Lupin expects to file gSpiriva DPI and gAdvair DPI during FY18 and FY19, respectively. Management expects the inhalation filings to get commercialized FY20 onwards. For gAdvair, Lupin is conducting additional PK studies factoring in complete response letters to Mylan and Hikma.
- Human biostudies on complex injectables are likely to commence shortly in the next few quarters. The company is currently developing four long acting injectables. The first long acting injectable filing is expected in FY19.
- On Biosimilars the company expects to file for Etanercept in FY18 in Europe and in FY19. Other products under development are PegGCSF and Reslizumab.
- On Specialty, the company's focus area includes Women Health, CNS and Pediatrics. Lupin will look to build its speciality portfolio largely through inorganic route. The company intends to consider commercialized, Phase 3 ready/completed (late stage) assets.

# Appendix A-1

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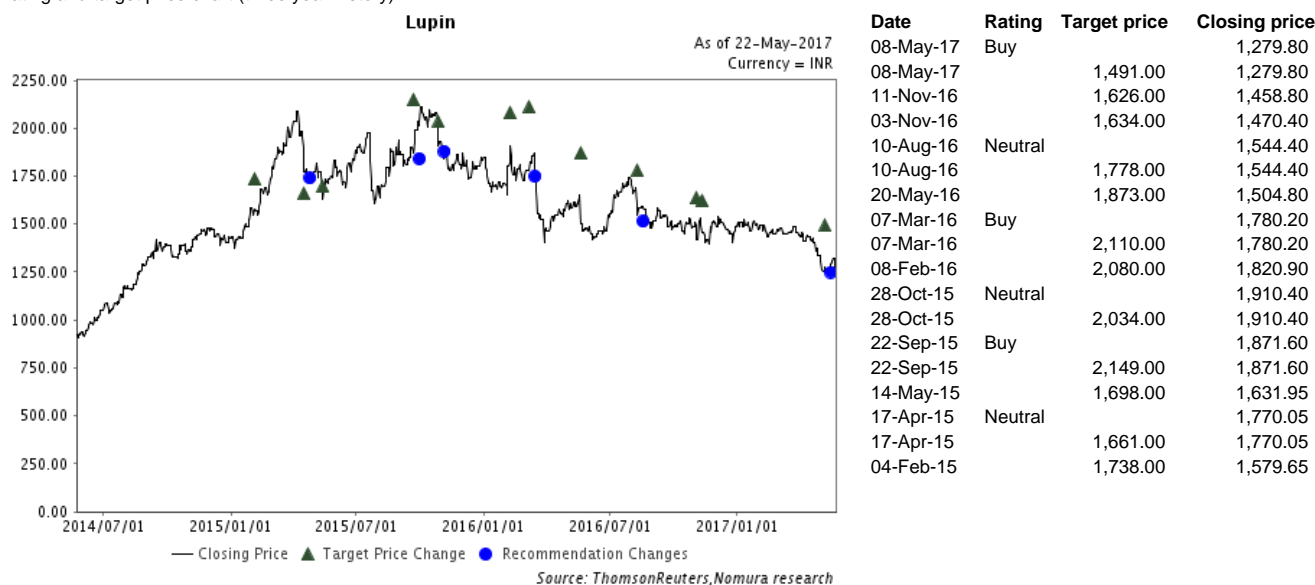
## Materially mentioned issuers

Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Lupin	LPC IN	INR 1228	24-May-2017	Buy	N/A	

### Lupin (LPC IN)

INR 1228 (24-May-2017) Buy (Sector rating: N/A)

Rating and target price chart (three year history)



For explanation of ratings refer to the stock rating keys located after chart(s)

**Valuation Methodology** We attribute 19x March 2019F EPS to arrive at our target price of INR1,491. The benchmark index for this stock is MSCI India.

**Risks that may impede the achievement of the target price** Key risks: 1) delay in approval of key products; 2) adverse currency movement; and 3) adverse regulatory developments.

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