

## The declining Metformin franchise

Lupin presented a grim outlook for FY18, given the price environment in the US market and continuing decline in the company's two key products, Glumetza and Fortamet. FY18 new launches in the US will just about offset price erosion in the base business excluding these two large products. Lupin needs to conduct additional studies before it can file gAdvaair in the US, now expected by FY19. We cut FY18/FY19 EPS estimates by 23%/10%. Maintain ADD.

**Muted outlook for the US business:** Lupin's US revenue declined 13% QoQ (drop of USD40mn), led by price erosion in Glumetza and Fortamet. With both these products expected to face further price erosion in FY18 and new launches expected to just about offset the price erosion in the base business, we believe Lupin's US business will decline 14-15% in FY18. Lupin has guided to maintaining its current R&D expense in absolute terms. This along with the price erosion in the US base will lead to pressure on Ebitda margins. We believe the company's FY18 EPS will be sharply lower than the FY17 EPS.

**FY18 launch pipeline is thin:** Although Lupin expects to launch >30 products in the US in FY18, most of these products will be small contributors to the company's US revenues. The only decent products are Minastrin, Epzicom and Bupropion HCL, which we have already built into our estimates. The Colesevelam/Sevelamer product lines are further pushed back with the launch now expected only by end-FY19, as the company needs to do additional work on both the API and formulation of these products.

**Limited progress on the gAdvaair project:** Lupin needs to conduct additional PK studies on gAdvaair, given recent developments at the competitors' projects (Mylan and Hikma's CRL). Lupin's product is expected to go into pivotal PK studies only in 2HCY17 and the company expects to file the product with USFDA by early FY19. However, we believe that CRLs of competitors and Teva's lower pricing for a similar product pose challenges to Lupin's filing timelines.

## Result update

CMP	Rs1228
12-mth TP (Rs)	1180 (-4%)
Market cap (US\$m)	8,550
Enterprise value(US\$m)	9,511
Bloomberg	LPC IN
Sector	Pharma

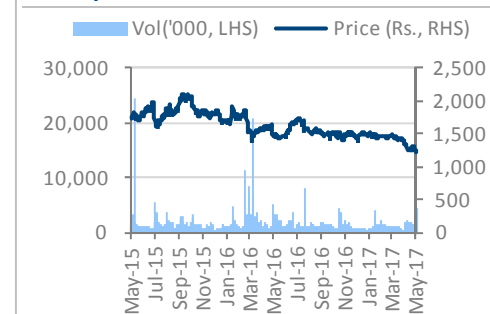
## Shareholding pattern (%)

Promoter	46.7
FII	31.9
DII	9.1
Others	12.3
52Wk High/Low (Rs)	1750/1168
Shares o/s (m)	452
Daily volume (US\$ m)	21.9
Dividend yield FY17ii (%)	0.6
Free float (%)	53.3

## Price performance (%)

	1M	3M	1Y
Absolute (Rs)	(9.8)	(15.3)	(16.2)
Absolute (US\$)	(13.1)	(13.8)	(12.3)
Rel. to Sensex	(12.0)	(20.2)	(36.0)
Cagr (%)	3 yrs	5 yrs	
EPS	19.8	21.1	

## Stock performance



## Financial summary (Rs m)

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
Revenues (Rs m)	127,700	142,555	174,943	173,573	195,005
Ebitda margins (%)	29.2	25.9	27.8	23.5	25.4
Pre-exceptional PAT (Rs m)	24,032	22,607	25,575	22,038	28,285
Reported PAT (Rs m)	24,032	22,607	25,575	22,038	28,285
Pre-exceptional EPS (Rs)	53.2	49.9	56.5	48.2	61.7
Growth (%)	31.2	(6.1)	13.2	(14.7)	28.1
IIFL vs consensus (%)			(20.2)	(40.6)	(44.1)
PER (x)	23.1	24.6	21.7	25.5	19.9
ROE (%)	30.2	22.5	20.7	15.3	17.1
Net debt/equity (x)	(0.2)	0.6	0.4	0.3	0.1
EV/Ebitda (x)	14.4	16.7	12.5	14.6	11.8
Price/book (x)	6.2	4.9	4.1	3.6	3.1

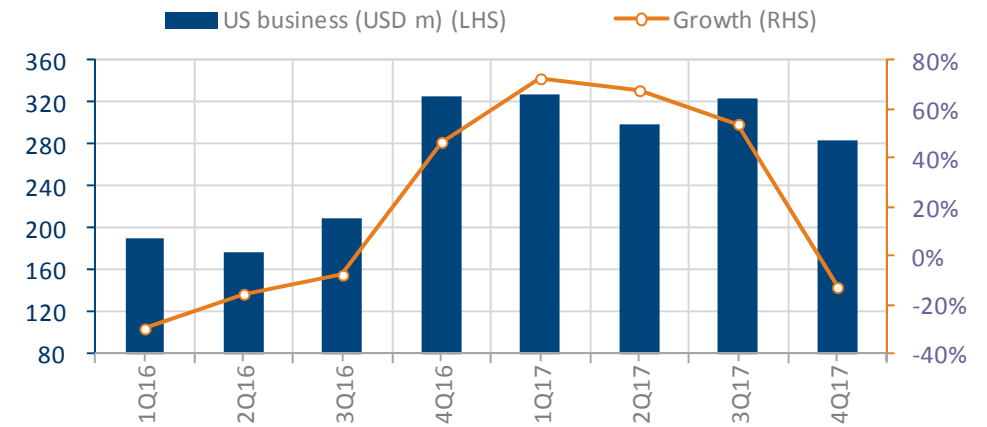
Source: Company, IIFL Research. Priced as on 24 May 2017

**Figure 1: Lupin’s 4QFY17 result – Operational results were in-line with our estimates after adjusting for the forex loss and provision for liability towards patent litigation**

Rs mn except EPS (based on Ind-AS)	4QFY16	3QFY17	4QFY17	YoY	QoQ
<b>Sales break-up</b>					
US	21,901	21,755	19,007	-13%	-13%
India	7,722	9,912	8,788	14%	-11%
Japan	3,442	4,492	4,672	36%	4%
South Africa	1,135	1,110	1,642	45%	48%
RoW	3,937	4,096	4,695	19%	15%
API business	2,953	2,684	2,815	-5%	5%
Net Sales	41,090	44,049	41,619	1%	-6%
Other operating income	884	779	914	3%	17%
<b>Total Revenue</b>	<b>41,974</b>	<b>44,829</b>	<b>42,533</b>	<b>1%</b>	<b>-5%</b>
Raw material costs	(11,010)	(13,016)	(11,851)	8%	-9%
Employee costs	(5,682)	(7,286)	(7,078)	25%	-3%
R&D expenses	(5,113)	(5,682)	(6,709)	31%	18%
Manufacturing & other expenses	(7,022)	(6,662)	(5,843)	-17%	-12%
<b>Ebitda</b>	<b>13,148</b>	<b>12,183</b>	<b>11,053</b>	<b>-16%</b>	<b>-9%</b>
<b>Ebitda margins</b>	<b>31.3%</b>	<b>27.2%</b>	<b>26.0%</b>	<b>-534 bps</b>	<b>-119 bps</b>
Depreciation & Amortisation	(1,487)	(2,309)	(2,674)	80%	16%
Interest & Finance charges	(311)	(484)	(406)	31%	-16%
<b>Other income*</b>	<b>349</b>	<b>1,036</b>	<b>(2,785)</b>	<b>-898%</b>	<b>-369%</b>
PBT	11,699	10,426	5,187	-56%	-50%
Taxes	(4,188)	(4,095)	(1,367)	-67%	-67%
Tax rate	35.8%	39.3%	26.4%	-944 bps	-1292 bps
Minority Interest/JV profit share	(33)	0	(18)	-45%	-9000%
<b>PAT</b>	<b>7,479</b>	<b>6,331</b>	<b>3,802</b>	<b>-49%</b>	<b>-40%</b>
Diluted shares outstanding	453.1	452.6	452.6	0%	0%
Diluted EPS	16.5	14.0	8.4	-49%	-40%

Source: Company, IIFL Research; Note – \*We have included forex loss of Rs1.7bn and provision for patent litigation liability of Rs1.6bn in other income

**Figure 2: Lupin’s US business declined sequentially by USD40mn in 4QFY17**



Source: Company, IIFL Research

**Figure 3: We have cut Lupin’s FY18/FY19 EPS estimates by 23%/10% respectively**

Estimates Revision	FY18ii	FY19ii
Total Revenue - old	191,115	207,889
Total Revenue - new	173,573	195,005
<b>% Change in Revenue</b>	<b>-9%</b>	<b>-6%</b>
Ebitda - old	48,345	52,957
Ebitda - new	40,837	49,585
<b>% Change in Ebitda</b>	<b>-16%</b>	<b>-6%</b>
Diluted EPS - old	62.6	68.9
Diluted EPS - new	48.2	61.7
<b>% Change in EPS</b>	<b>-23%</b>	<b>-10%</b>

Source: Company, IIFL Research

**Background:** Lupin, the second largest Indian pharma company in terms of market capitalisation, actively targets the generics opportunity in regulated markets. Currently, the chronic-therapy business contributes 66% of total revenue in the domestic market, which makes Lupin a strong player in the specialties segment. Lupin has emerged as a fully-integrated company, with manufacturing capabilities in APIs and formulations and a direct marketing presence in its target markets, including the US, Europe and Japan. In the US market, apart from being one of the fastest-growing companies in the generic space, Lupin is also one of the few Indian companies to have a strong presence in the branded generics segment as well.

## Management

Name	Designation
Dr. Kamal K Sharma	Vice Chairman
Vinita Gupta	CEO
Nilesh Gupta	MD

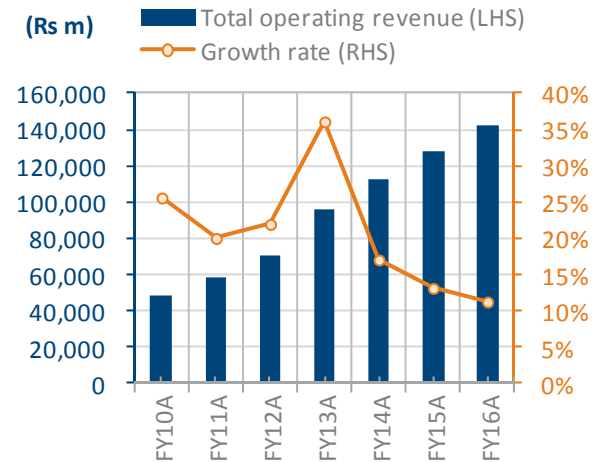
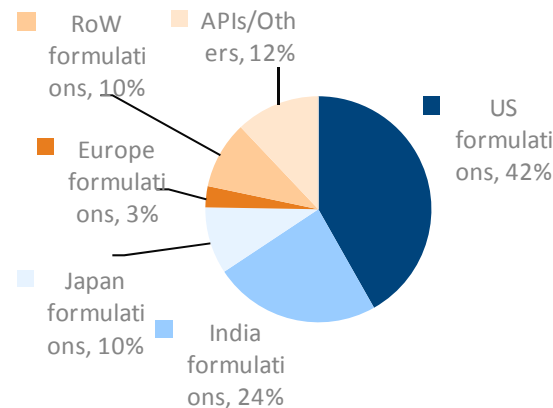
Sun Pharma, Dr. Reddy's, Cipla, Cadila, Glenmark:

## Assumptions

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
US business growth (%)	15.8	4.7	39.5	(17.7)	13.5
Japanese business growth (%)	2.2	3.1	30.2	26.3	10.0
Domestic growth (%)	19.7	16.2	10.6	14.0	14.0
API business growth (%)	7.2	4.4	(8.7)	5.0	5.0
EBITDA margin (%)	29.2	25.9	27.8	23.5	25.4
Tax rate (%)	28.4	31.9	27.7	25.0	25.0

Source: Company data, IIFL Research

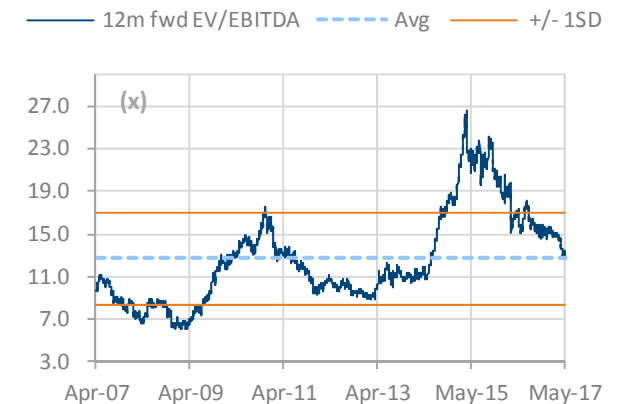
## Revenue break-up - FY16



## PE Chart



## EV/Ebitda



## Financial summary

### Income statement summary (Rs m)

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
<b>Revenues</b>	<b>127,700</b>	<b>142,555</b>	<b>174,943</b>	<b>173,573</b>	<b>195,005</b>
Ebitda	37,342	36,854	48,620	40,837	49,585
Depreciation and amortisation	(4,347)	(4,871)	(9,122)	(11,368)	(12,787)
Ebit	32,995	31,982	39,498	29,469	36,798
Non-operating income	1,252	1,852	(2,624)	1,407	2,016
Financial expense	(98)	(595)	(1,525)	(1,590)	(1,226)
PBT	34,148	33,239	35,349	29,286	37,588
Exceptionals	0	0	0	0	0
Reported PBT	34,148	33,239	35,349	29,286	37,588
Tax expense	(9,704)	(10,593)	(9,785)	(7,321)	(9,397)
PAT	24,444	22,646	25,564	21,964	28,191
Minorities, Associates etc.	(412)	(39)	11	73	94
<b>Attributable PAT</b>	<b>24,032</b>	<b>22,607</b>	<b>25,575</b>	<b>22,038</b>	<b>28,285</b>

### Ratio analysis

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
<b>Per share data (Rs)</b>					
Pre-exceptional EPS	53.2	49.9	56.5	48.2	61.7
DPS	7.5	7.5	7.5	7.5	7.5
BVPS	198.0	248.5	299.6	338.5	390.9
<b>Growth ratios (%)</b>					
Revenues	13.1	11.6	22.7	(0.8)	12.3
Ebitda	24.4	(1.3)	31.9	(16.0)	21.4
EPS	31.2	(6.1)	13.1	(14.7)	28.1
<b>Profitability ratios (%)</b>					
Ebitda margin	29.2	25.9	27.8	23.5	25.4
Ebit margin	25.8	22.4	22.6	17.0	18.9
Tax rate	28.4	31.9	27.7	25.0	25.0
Net profit margin	19.1	15.9	14.6	12.7	14.5
<b>Return ratios (%)</b>					
ROE	30.2	22.5	20.7	15.3	17.1
ROCE	38.2	23.2	17.5	13.6	16.8
<b>Solvency ratios (x)</b>					
Net debt-equity	(0.2)	0.6	0.4	0.3	0.1
Net debt to Ebitda	(0.4)	1.7	1.1	1.0	0.5
Interest coverage	NM	NM	25.9	18.5	30.0

Source: Company data, IIFL Research

### Balance sheet summary (Rs m)

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
Cash & cash equivalents	21,372	8,238	28,135	21,218	17,862
Inventories	25,036	32,737	36,423	36,450	40,951
Receivables	26,566	45,488	43,073	45,129	50,701
Other current assets	5,350	12,412	11,910	13,265	16,052
Creditors	27,166	30,737	33,449	35,116	39,048
Other current liabilities	5,743	2,348	4,714	3,550	4,184
<b>Net current assets</b>	<b>45,415</b>	<b>65,789</b>	<b>81,379</b>	<b>77,397</b>	<b>82,335</b>
Fixed assets	32,031	60,516	67,694	71,326	73,539
Intangibles	17,411	53,678	63,966	63,966	63,966
Investments	25	143	220	220	220
Other long-term assets	3,587	13,038	14,651	14,651	14,651
<b>Total net assets</b>	<b>98,469</b>	<b>193,164</b>	<b>227,910</b>	<b>227,561</b>	<b>234,711</b>
Borrowings	5,402	71,266	79,521	61,284	44,329
Other long-term liabilities	4,085	9,943	13,068	13,068	13,068
<b>Shareholders equity</b>	<b>88,982</b>	<b>111,955</b>	<b>135,321</b>	<b>153,209</b>	<b>177,314</b>
<b>Total liabilities</b>	<b>98,469</b>	<b>193,164</b>	<b>227,910</b>	<b>227,561</b>	<b>234,711</b>

### Cash flow summary (Rs m)

Y/e 31 Mar, Consolidated	FY15A	FY16A	FY17ii	FY18ii	FY19ii
Ebit	32,995	31,982	39,498	29,469	36,798
Tax paid	(9,436)	(11,662)	(9,785)	(7,321)	(9,397)
Depreciation and amortization	4,347	4,871	9,122	11,368	12,787
Net working capital change	(949)	(31,537)	4,308	(2,936)	(8,293)
Other operating items	374	2,655	0	0	0
Operating cash flow before interest	27,331	(3,690)	43,143	30,580	31,895
Financial expense	(109)	(436)	(1,525)	(1,590)	(1,226)
Non-operating income	1,242	2,397	7,663	1,407	2,016
<b>Operating cash flow after interest</b>	<b>28,463</b>	<b>(1,729)</b>	<b>49,281</b>	<b>30,396</b>	<b>32,685</b>
<b>Capital expenditure</b>	<b>(8,676)</b>	<b>(57,746)</b>	<b>(18,000)</b>	<b>(15,000)</b>	<b>(15,000)</b>
Long-term investments	(6,294)	(12,223)	(10,050)	0	0
Others	0	0	0	0	0
<b>Free cash flow</b>	<b>13,493</b>	<b>(71,697)</b>	<b>21,231</b>	<b>15,396</b>	<b>17,685</b>
Equity raising	413	536	0	0	0
Borrowings	(700)	62,081	2,739	(18,238)	(16,955)
Dividend	(1,573)	(4,055)	(4,072)	(4,076)	(4,086)
Net chg in cash and equivalents	11,633	(13,135)	19,898	(6,918)	(3,356)

Source: Company data, IIFL Research

**Disclosure : Published in 2017, © India Infoline Ltd 2017**

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In addition, **Add** and **Reduce** recommendations are based on expected returns relative to a hurdle rate. Investment horizon for **Add** and **Reduce** recommendations is up to a year. We assume the current hurdle rate at 10%, this being the average return on a debt instrument available for investment.

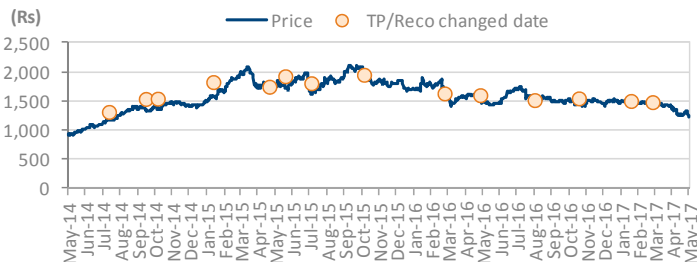
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**Lupin: 3 year price and rating history**



Date	Close price (Rs)	Target price (Rs)	Rating	Date	Close price (Rs)	Target price (Rs)	Rating
08 May 2014	990	1056	ADD	10 Nov 2016	1530	1545	ADD
04 Aug 2014	1165	1312	ADD	10 Feb 2017	1491	1500	ADD
08 Oct 2014	1368	1535	BUY	20 Mar 2017	1457	1480	ADD
29 Oct 2014	1358	1540	BUY				
04 Feb 2015	1546	1825	BUY				
14 May 2015	1690	1745	BUY				
11 Jun 2015	1795	1925	BUY				
27 Jul 2015	1672	1805	BUY				
28 Oct 2015	1946	1950	BUY				
18 Mar 2016	1674	1630	ADD				
20 May 2016	1655	1600	ADD				
24 Aug 2016	1556	1515	ADD				