

EBITDA ahead of estimates (Erratum)

Quick Note

This note replaces an earlier published report which incorrectly indicated that “the stock currently trades at P/E of 17.5x and 15.5x on FY18F and FY19F EPS of INR58.5 and INR65.8”. We apologise for any inconvenience this may have caused.

Fig. 1: Quarterly result

Above or below	2QFY18 operating performance was ahead of our estimates. EBITDA at INR8.5bn vs. our estimate of INR7.2bn. Net profit at INR4.55bn (vs. estimate of INR 3.33bn).
What to make of it	The stronger operating performance was despite a weak US revenue which declined USD34mn q-q. Strong growth in ROW markets, cost control (R&D and other expenses declining y-y) and forex gain of INR420mn led to higher-than-estimated net earnings.
Key numbers	US revenues at USD204mn (estimate: USD215mn) as pricing pressure continues. India growth at 20% y-y adjusted for GST tax adjustments. EBITDA margin at 21.6% vs. 19.9% in 1QFY18 and 24% in 2QFY17.
What next	Stability in the US business and new launched hold the key. There are no positive surprises on new launches so far. Successful development, filing and approval of key inhalers, complex injectables can be potential value drivers of Lupin.

Source: Company data, Nomura estimates

LPC’s 2QFY18 results were better than our expectations at the operating level. EBITDA at INR8.5bn was ahead of our estimates of INR7.2bn. The outperformance at operating level was despite weaker US sales, which declined more than our expectation. US sales declined USD34mn q-q to USD204mn. The management expects the US sales to form a base at the 2QFY18 levels and grow from here over time. The substantial decline in gFortamet and gGlumetza in the recent past is arrested for the time being. We believe timely launch of new products in the US is key as further erosion in base over time due to additional competition in gFortamet and gGlumetza and some more impact of channel consolidation. The management commentary didn’t present any positive surprise with respect to new launches. The efforts on cost containment (R&D and other expenditure) helped negate the impact of lower US revenues.

We have a Buy rating on Lupin. Our 12-month TP of INR1,181/sh is based on 19x FY19-20F average EPS of INR62.1. The stock currently trades at P/E of 17.5x and 15.5x on FY19F and FY20F EPS of INR58.5 and INR65.8, respectively.

Key highlights from result and post result conference call

- North America sales: NA revenues declined to USD204mn from USD238mn in 1QFY18. Sales were lower than our estimate of USD 215mn. The decline was driven by lower realisation on account of channel consolidation, price erosion and volume loss in gFortamet, gGlumetza and gMinastrin 24Fe. The Gavis business has recorded increase Q-Q. The management expects, 2QFY18 sales to form the base and sales can

Global Markets Research

31 October 2017

Rating Remains	Buy
Target Price Remains	INR 1181
Closing price 30 October 2017	INR 1026

Research analysts

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gradually rise from the current levels. Sales of gFortamet and gGlumetza have now stabilised as per management. We highlighted in our report "US sales review" that pricing on both the products have stabilised for the time being. We do expect additional competition and fall in sales over time. Key product launches: The key product launches in FY18F and FY19F include gAxiiron, Levothyroxine tabs, gTamiflu and gRanexa. For other key known products – gPrevacid ODT, gLlalda, gCoregCR and gWelchol – there are pending CRLs that are being addressed. These launches are likely only towards end FY19F. There is a delay in launches in these products compared to earlier management commentary. Launch delays can substantially reduce the sales opportunity for Lupin, in our view.

- Complex generics: The company has pruned its ANDA development pipeline to focus more on complex generic products. We believe progress in inhalers is key, which can differentiate Lupin over the next 2-3 years. The most near-term high-value prospect is gPro Air, which presents a USD1.2bn market. The management continues to expect launch in FY20F post expiry of the 30-month stay. The product has a TAD (target action date) in mid 2018 (we expected it by end 2017). Lupin is the second generic known generic filer for gProAir after Perrigo.

On gAdvair, the company addressed the issue of batch to batch variability and will conduct PK (pharmacokinetic) studies before proceeding to Phase III clinical trials in end FY18F.

The clinical trials for gSpiriva are likely to end in FY18F, post which the company expects to make ANDA filing. Lupin is likely to be the first ANDA filer for gSpiriva.

On long acting injectables, the company expects to repeat human PK studies, post which clinical trials are likely to commence.

- India formulation: India formulation recorded a growth of 16.4% y-y. However, adjusted for GST (the sales now reported in net of GST), the sales growth was at 20% y-y on a like to like basis. The strong growth during the quarter was on account of channel restocking. The management expects the India market growth at ~15% over the next two quarters.
- R&D spend: The R&D spend for the quarter at INR4.74bn was down 13% y-y. The company expects to file 30 ANDAs in FY18F including 4-5 injectable filings. The company has filed 11 ANDAs in 1HFY18, including 10 in 2QFY18.
- Other expenses: The other expenses are down 17% y-y. This is driven by lower R&D spend and lower indirect taxes (which is now entirely netted off against the sales).
- Guidance maintained: The management has guided towards 21-23% EBITDA margin and a single-digit decline in sales in FY18F. With rise in US sales and cost control initiatives, the management expects margins to rise in FY19F.

Fig. 2: Quarterly results

Revenue split	2QFY17	1QFY18	2QFY18	Y-Y Chg (%)	Q-Q Chg (%)	2QFY18 Nom ests	vs Nom ests (%)
Formulations	39,193	35,275	36,092	-7.9%	2.3%	37,228	-3.1%
North America	19,978	16,018	13,611	-31.9%	-15.0%	14,830	-8.2%
India	9,958	9,324	11,593	16.4%	24.3%	12,149	-4.6%
Japan	4,384	4,981	5,057	15.3%	1.5%	4,877	3.7%
Others	4,873	4,952	5,831	19.7%	17.7%	5,372	8.5%
API	2,919	2,793	2,650	-9.2%	-5.1%	2,800	-5.4%
Total Sales	42,112	38,068	38,742	-8.0%	1.8%	40,028	-3.2%
P&L							
	2QFY17	1QFY18	2QFY18	Y-Y Chg (%)	Q-Q Chg (%)	2QFY18 Nom ests	vs Nom ests (%)
Net Sales	42,112	38,068	38,742	-8.0%	1.8%	40,028	-3.2%
Other Operating Income	794	628	778	-2.0%	24.0%	650	19.7%
Total Revenue	42,906	38,696	39,520	-7.9%	2.1%	40,678	-2.8%
Material Cost	12,429	12,326	12,865	3.5%	4.4%	13,501	-4.7%
Staff Cost	7,124	7,180	7,250	1.8%	1.0%	7,246	0.1%
Other Expense	13,072	11,506	10,874	-16.8%	-5.5%	12,727	-14.6%
EBITDA	10,281	7,684	8,531	-17.0%	11.0%	7,203	18.4%
Other Income	271	320	740	173.1%	131.6%	350	111.5%
Interest Expense	263	439	479	82.2%	9.2%	440	8.9%
Depreciation	2,112	2,605	2,722	28.9%	4.5%	2,650	2.7%
PBT	8,177	4,959	6,070	-25.8%	22.4%	4,463	36.0%
Tax	1,589	1,368	1,541	-3.1%	12.6%	1,116	38.1%
Net Profit	6,588	3,591	4,529	-31.2%	26.1%	3,347	35.3%
Minority interest	8	(12)	19			10.00	
Share of Profit from JVs	42	(23)	39				
Net profit after MI	6,622	3,581	4,550	-31.3%	27.1%	3,337	36.3%
				bps Chg (Y-Y)	bps Chg (Q-Q)		vs Nom ests
Gross margin (%)	70.5%	67.6%	66.8%	(369)	(83)	66.3%	52
EBITDA margin (%)	24.0%	19.9%	21.6%	(238)	173	17.7%	388
Tax rate (%)	19.4%	27.6%	25.4%	594	(221)	25.0%	38

Source: Company data, Nomura estimates

Appendix A-1

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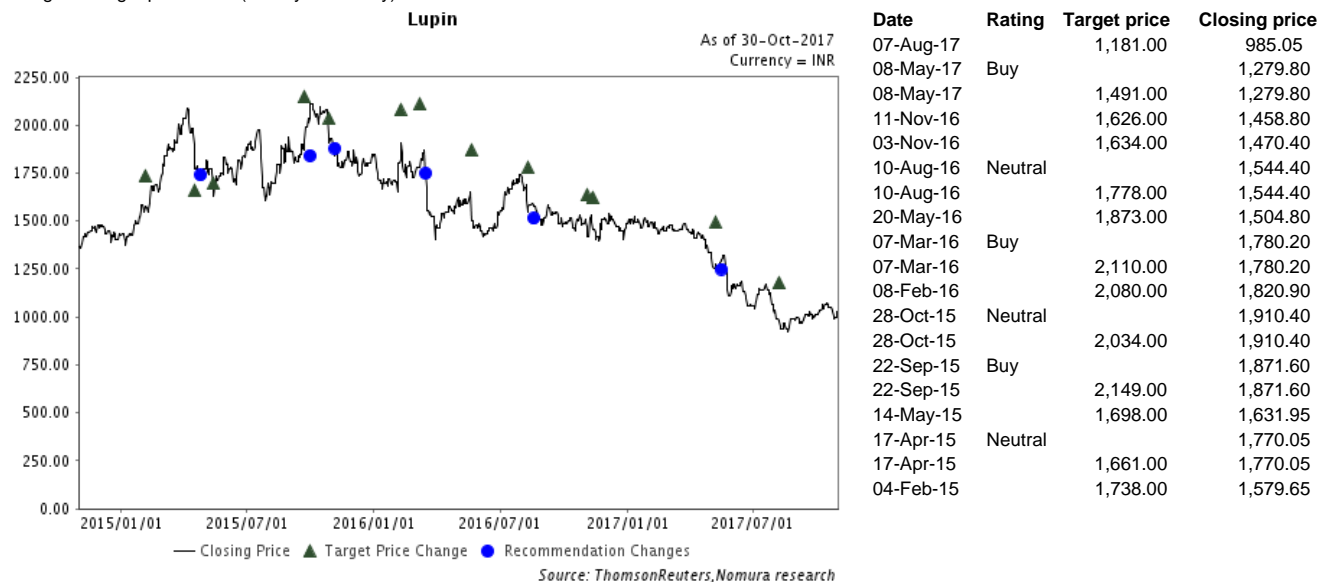
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Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Lupin	LPC IN	INR 1026	30-Oct-2017	Buy	N/A	

Lupin (LPC IN)

INR 1026 (30-Oct-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 arrive at our 12-month TP of INR1,181/sh based on 19x FY19-20F average EPS of INR 62.1. 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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As at 30 September 2017.

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