



Lupin (LUPN.BO)

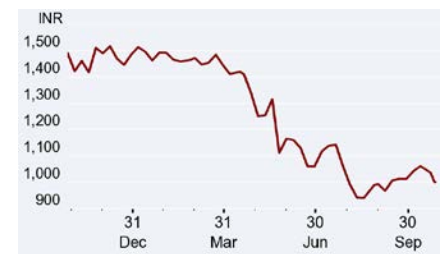
Results: 2Q Beat, US Erosion takes the Shine Off

- Citi's Take** — 2Q numbers beat expectations (c.8% on EBITDA) but it was not all smooth sailing. Restocking in India and lower R&D/Sales were the key drivers of the beat but pressure on the US business continues (sharp QoQ decline) and we do not see any material launch in the near term that could offset the decline in its larger products. On the positive side, the company reiterated its FY18 EBITDA margin guidance of c.21-23%, as operational efficiencies help offset some of the US pricing pain.
- Steep Erosion in US sales** — US sales declined c.US\$34m QoQ as Lupin's top products (Glumetza and Fortamet) faced further price erosion and Minastrin 24Fe also saw competition post exclusivity. Base business sales also declined as supply chain consolidation continues to impact. Lupin expects high single digit price erosion in FY18 in its base business.
- Delivery on US launches is key to FY19 growth** — Though Lupin has several interesting products in the pipeline, execution is critical for growth in FY19. The management expects to launch Levothroxine, Axiron and Tamiflu in late FY18 and certain FTFs (Ranexa, Solodyn) and two mesalamine products (Apriso, Lialda) in FY19. The Renvela opportunity appears to have become less attractive as competition has entered ahead of Lupin.
- Calibrated approach towards R&D** — Lupin maintained that it would calibrate its R&D efforts. It has pruned some oral solids from the pipeline but reiterated that it is unlikely to compromise on key assets. R&D spend was at 12% of revenue in 2Q and is expected to remain this range as per management.
- Implications** — We cut our FY18/19/20E EPS by 9.5%/9.2%/7.6% to reflect lower US sales. Our new target price is Rs1,240/sh as we roll over to 20x March '19E EPS vs. 20x Sept'18E earlier.

- Estimate Change
- Target Price Change

Buy	1
Price (30 Oct 17 15:30)	Rs1,027.55
Target price	Rs1,240.00
	from Rs1,170.00
Expected share price return	20.7%
Expected dividend yield	0.7%
Expected total return	21.4%
Market Cap	Rs464,286M
	US\$7,138M

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



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2016A	22,955	50.78	-4.5	20.2	4.2	23.1	0.7
2017A	26,702	59.07	16.3	17.4	3.4	21.8	0.7
2018E	19,753	43.69	-26.0	23.5	3.1	13.8	0.7
2019E	27,885	61.68	41.2	16.7	2.6	17.2	0.7
2020E	34,869	77.13	25.0	13.3	2.2	18.4	0.7

Source: Powered by dataCentral

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Figure 1. Lupin - 2Q headline numbers

Headline Numbers		Key Regions (Growth)		Operational Metrics	
Revenues	-8%	US	-31.9%	R&D (% of Sales)	12%
EBIDTA	-21%	India	16.4%	ANDAs filed / total	10 / 152
Adj. Net Income	-37%	APAC	15.2%	ANDA approvals/ total	9 / 225
Adj. EBIDTA Margin	21.6% (-363bps)	EMEA	17.1%	FTFs / Sole FTFs	49 / 25

Source: Company data, Citi Research

Top-line was largely in-line as strong India (partly due to re-stocking) and Ex US Exports have contained the impact of a sharp decline in US revenues.

Domestic sales have grown by 16% YoY and (c20% on like to like basis, adj to GST accounting).

High offtake in India, lower R&D and operating efficiencies have helped in QoQ improvement in EBITDA margins.

Other income includes forex gain of c.Rs300m.

Figure 2. Lupin – 2QFY18 Consolidated Income Statement (Rs m, %)

	2QFY17	2QFY18	% Ch YoY	1QFY18	% Ch QoQ
Net Sales	42,112	38,742	(8.0)	38,068	1.8
Other Operating Income	793	778	(1.9)	628	24.0
Total Revenues	42,905	39,520	(7.9)	38,696	2.1
Raw material cost	12,429	12,865	3.5	12,326	4.4
as a % sales	29.0	32.6	359 bps	31.9	70 bps
Staff cost	7,124	7,250	1.8	7,180	1.0
as a % sales	16.6	18.3	174 bps	18.6	-21 bps
Other expenditure	12,532	10,874	(13.2)	11,505	(5.5)
as a % sales	29.2	27.5	-169 bps	29.7	-222 bps
Total expenditure	32,084	30,989	(3.4)	31,011	(0.1)
EBITDA	10,821	8,531	(21.2)	7,685	11.0
EBITDA Margins (%)	25.2	21.6	-363 bps	19.9	173 bps
Depreciation	2,112	2,722	28.9	2,605	4.5
Interest	263	479	82.2	440	8.9
Other Income	271	740	173.1	320	131.6
PBT	8,717	6,070	(30.4)	4,959	22.4
Tax	1,589	1,541	(3.1)	1,368	12.6
Effective Tax Rate (%)	18.2	25.4	715 bps	27.6	-221 bps
Minority Interest	(34)	(20)	(40.7)	11	(292.5)
Recurring PAT	7,162	4,550	(36.5)	3,581	27.1
EO expense/(income) items	540	-		-	
Reported PAT	7,702	4,550	(40.9)	3,581	27.1

Source: Company data, Citi Research

Figure 3. Lupin – 2QFY18 Revenue Breakdown (Rs m)

	2QFY17	2QFY18	% Ch YoY	1QFY18	% Ch QoQ
Formulations	39,193	36,092	(7.9)	35,275	2.3
% of Total Sales	93.1	93.2		92.7	
North America	19,978	13,611	(31.9)	16,018	(15.0)
India	9,958	11,593	16.4	9,324	24.3
Asia Pacific	5,520	6,357	15.2	5,989	6.1
EMEA	2,355	2,758	17.1	2,259	22.1
LATAM	986	1,395	41.5	1,269	9.9
ROW	396	378	(4.5)	416	(9.1)
APIs	2,919	2,650	(9.2)	2,793	(5.1)
% of Total Sales	6.9	6.8		7.3	
Total	42,112	38,742	(8.0)	38,068	1.8

Source: Company data, Citi Research

Figure 4. Earnings Revision

EPS	FY18E	FY19E	FY20E
New	43.7	61.7	77.1
Old	48.3	68.0	83.5
Change (%)	-9.5%	-9.2%	-7.6%

Source: Citi Research

Lupin

Valuation

We value Lupin at Rs1,240, based on 20x Mar'19E EPS. Our target multiple is derived from 1) a 13x P/E for the US generics business, set at a 15-20% discount to mid-sized US generics players given the high risk to a couple of in-market products; 2) a 28x P/E for the India business, ascribing a 20-25% premium to the 12M forward consensus-based P/E for Alkem, a close pure-India comparable, to reflect its market leadership and good growth; and 3) 18x for Others businesses (ex. India and the US, including APIs). The 18x is in-line with the 16-19x P/E range for emerging-market peers. We then apply a +5% adjustment factor to account for the company's relatively healthy profitability/Rol.

Risks

Key risks that could impede the stock from achieving our target price include: 1) Rising competitive intensity in its US business, given faster pace of approvals for the industry; 2) Delay in approval of products especially from the niche portfolio in the US; and 3) Inability to effectively scale up the Japanese operations would hurt one of the longer-term growth drivers.

Appendix A-1

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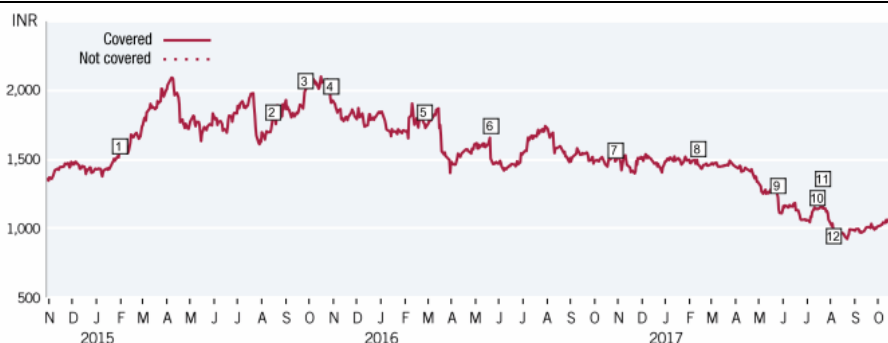
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Analyst: Prashant Nair, CFA



Date	Rating	Target Price	Closing Price
1 28-Jan-15 07:04:49	1	*2,020.00	1,513.35
2 13-Aug-15 19:53:45	1	*2,270.00	1,757.00
3 24-Sep-15 18:24:09	1	*2,550.00	1,989.45
4 27-Oct-15 17:42:15	1	*2,360.00	1,945.65

Date	Rating	Target Price	Closing Price
5 24-Feb-16 04:33:01	1	*2,130.00	1,762.15
6 19-May-16 21:28:11	1	*1,930.00	1,655.80
7 27-Oct-16 07:43:51	1	*1,970.00	1,485.00
8 09-Feb-17 12:58:13	1	*1,890.00	1,495.35

Date	Rating	Target Price	Closing Price
9 24-May-17 17:12:07	1	*1,630.00	1,227.65
10 13-Jul-17 08:52:17	1	*1,480.00	1,141.90
11 21-Jul-17 07:19:42	1	*1,350.00	1,142.85
12 03-Aug-17 13:14:36	1	*1,170.00	994.90

*Indicates Change

Rating/target price changes above reflect Eastern Time

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