

BSE SENSEX	S&P CNX
34,196	10,498
Bloomberg	LPC IN
Equity Shares (m)	451.6
M.Cap.(INRb)/(USD\$b)	362.2 / 5.7
52-Week Range (INR)	1572 / 790
1, 6, 12 Rel. Per (%)	-11/-23/-67
Avg Val, INRm	2021.0
Free float (%)	53.0

CMP: INR802 TP: INR940(+17%) Buy

Sequential improvement in US business; margin improvement will be key

- 3QFY18 revenue fell 11% YoY to INR39.8b (est. of INR40b). Gross margin shrunk 600bp YoY (-240bp QoQ) to 65%. EBITDA fell ~22% YoY to INR6.9b (est. of INR8.8b), with the margin contracting ~1,000bp YoY (-430bp QoQ) to ~17.3%. 3QFY18 EBITDA included a forex loss of ~INR821m v/s a gain of INR571m in 2Q and a gain of INR276m in 3QFY17. PAT fell 65% YoY to INR2.2b (est. of INR4.3b)
- **US business – recovery expected from 2HCY18:** US business sales came in at USD213m v/s USD204m in 2QFY18 and USD316m in 3QFY17. Pricing pressure in the base business was offset by recent launches and pick-up in branded business sales. US branded business grew ~25% YoY in 3Q. LPC plans to launch ~10 products in 4Q, including Tamiflu and Axiron. The company also plans to launch its branded product, Solosec, in 1QFY19.
- **Earnings call takeaways:** 1) Update on warning letter – hired consultants (Lachman and Parexel) to help with the remediation process; LPC plans to finish remediation work by April/May-18. 2) Metformin market share has settled down (although Nostrum and SUNP are yet to enter the market). 3) Remediation expense in 3QFY18 was not meaningful. 4) R&D expense to stay at ~12-12.2% in FY19E. 5) Levothyroxine approval expected by mid-CY18. 6) Etanercept filing – Japan & EU in 4Q FY18E and the US in FY19E.
- **Near-term pressure persists; stock factoring in most of the negatives:** LPC has invested ~INR60b toward R&D over FY16-18E (much higher than what it invested in a decade prior to that). GMP compliance is key to monetize this investment. Although the stock faces near-term pressure, key approvals in the US and resolution of the WL status (expected in 12 months) will help create value in 12-18 months. We maintain **Buy** with a TP of INR940 @ 20x 1HFY20E PER (v/s INR1,000 @20x 1HFY20E PER). We cut FY18E and FY19/20E EPS by ~6% and 5%, respectively, as we build in the cost impact.

Financials & Valuations (INR b)

Y/E Mar	2018	2019E	2020E
Net Sales	157.8	179.6	208.2
EBITDA	31.4	36.8	46.4
PAT	14.2	18.2	24.4
EPS (INR)	31.5	40.2	54.1
Gr. (%)	-44.4	27.7	34.6
BV/Sh (INR)	319.8	349.5	393.1
RoE (%)	10.2	12.0	14.6
RoCE (%)	7.0	8.4	10.3
P/E (x)	25.5	19.9	14.8
P/BV (x)	2.5	2.3	2.0

Estimate change



TP change

Rating change



Quarterly Performance (Consolidated)

Y/E March	FY17				FY18E				FY17	FY18E	% Var	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE	3QE			
Net Sales	44,677	42,905	44,828	42,533	38,696	39,520	39,756	39,826	174,943	157,798	40,027	-0.7
YoY Change (%)	41.6	28.9	26.1	2.0	-13.4	-7.9	-11.3	-6.4	23.1	-9.8	-10.7	
Total Expenditure	31,596	32,624	32,670	31,481	31,012	30,989	32,873	31,522	130,012	126,396	31,221	
EBITDA	13,080	10,281	12,158	11,052	7,684	8,531	6,883	8,304	44,931	31,402	8,806	-21.8
Margins (%)	29.3	24.0	27.1	26.0	19.9	21.6	17.3	20.9	25.7	19.9	22.0	
Depreciation	2,027	2,112	2,309	2,674	2,605	2,722	2,804	2,796	9,122	10,926	2,725	
Interest	320	263	459	406	439	479	540	526	1,525	1,984	600	
Other Income	826	271	1,036	453	320	740	284	306	1,065	1,650	350	
PBT	11,560	8,177	10,426	8,425	4,959	6,070	3,824	5,288	35,349	20,141	5,831	-34.4
Tax	2,734	1,589	4,095	1,367	1,368	1,541	1,608	1,325	9,785	5,841	1,545	
Rate (%)	23.7	19.4	39.3	16.2	27.6	25.4	42.0	25.0	27.7	29.0	26.5	
Minority Interest	6	8	24	-16	-12	19	5	74	72	85	20	
Recurring PAT	8,820	6,622	6,331	6,069	3,581	4,550	2,216	3,890	25,492	14,215	4,266	-48.0
YoY Change (%)	55.1	58.0	19.5	-18.9	-59.4	-30.8	-65.0	-35.9	12.3	-44.2	-32.6	
Margins (%)	19.7	15.4	14.1	14.3	9.3	11.5	5.6	9.8	14.6	9.0	10.7	

E: MOSL estimates; Quarterly nos will not add up to full year nos due to restatement of past quarters

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

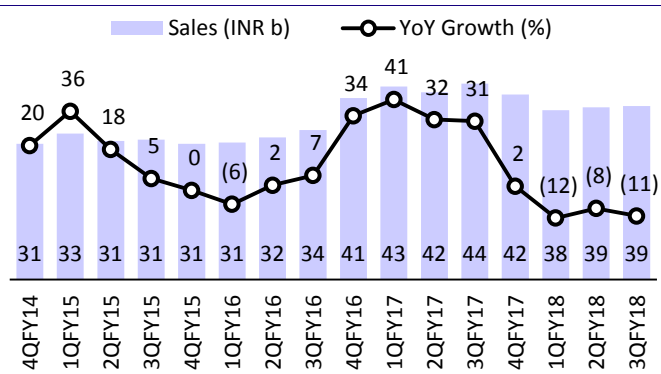
Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

US business improves sequentially; margin impacted by one-offs

Lupin's 3QFY18 net revenues declined ~12% YoY to INR39.8b (~1% below estimate). US business continued to decline significantly by ~34% YoY to INR14.3b (but grew ~5% QoQ), while India business grew ~8% YoY to INR10.7b (-8% QoQ). Apart from the US and India, LPC's other geographies saw robust growth, with RoW up 16%, South Africa up ~19% and Japan up ~23%. Europe business declined ~4% YoY.

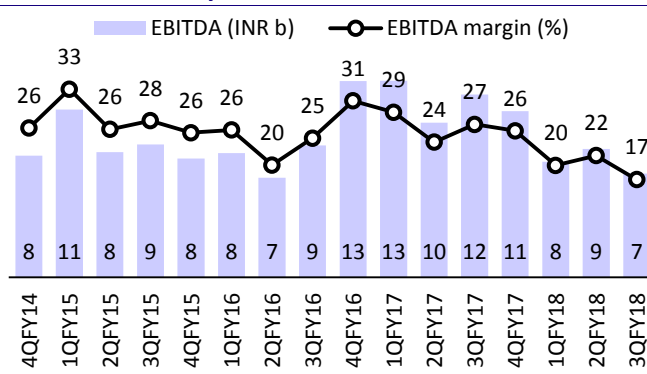
LPC's EBITDA declined significantly by ~43% YoY (-19% QoQ) due to change in business mix (more of India business than US) and a forex loss of INR821m (v/s gain of INR571m in 2Q and INR276m in 3QFY17). Margin came in at 17.3% (-1,000bp YoY and ~430bp QoQ). Margin after adjusting for forex loss was still behind our estimate of 22%, although management has guided for 21-22% margin for FY18/19.

Exhibit 1: Revenues declined 11% YoY



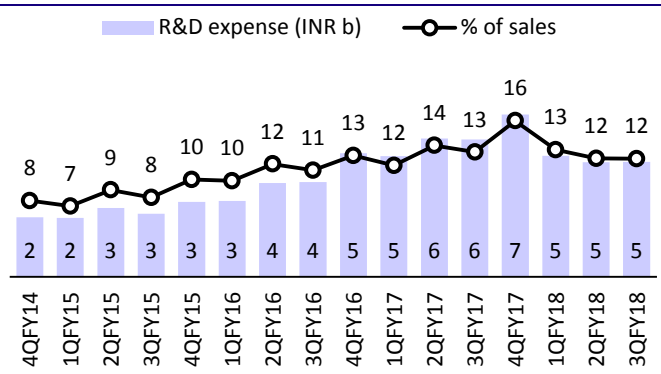
Source: Company, MOSL

Exhibit 2: Quarterly EBITDA trend



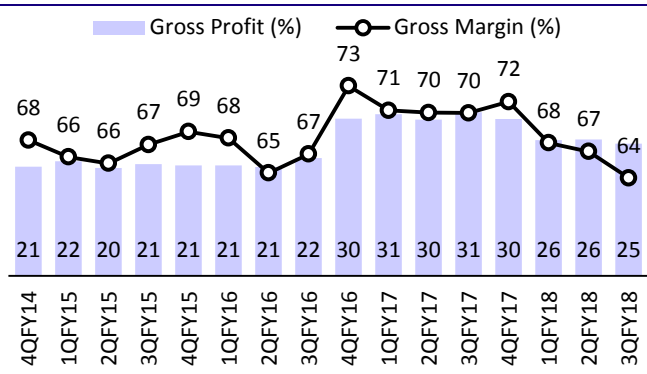
Source: Company, MOSL

Exhibit 3: R&D expense trend



Source: Company, MOSL

Exhibit 4: Gross margins to be in the range of 65-68%



Source: Company, MOSL

US Generic business - (37% of sales)

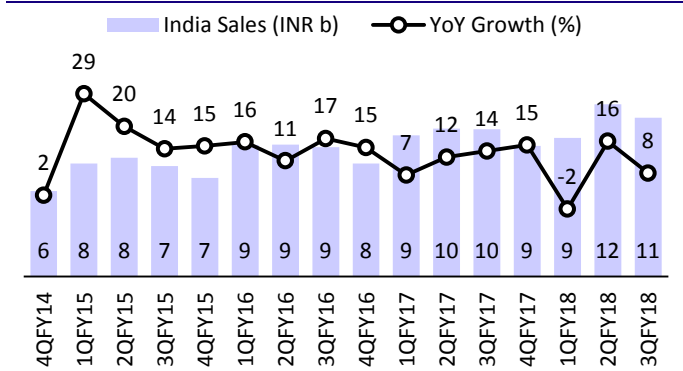
- US business declined 34%YoY to INR14.3b, primarily due to competition in base products, but increased sequentially driven by Fosrenol and Vigamox.
- Company expects US business to pick up 4QFY18 onwards on the back of new launches.
- During the quarter, US branded business by ~25% on the back of Methergine and contribution from new products as well (like Doxycycline Hyclate, Hydrocodone APAP).
- The company launched 3 products in the US in 3QFY18. Cumulatively, LPC is marketing 149 products in US market as of end-3QFY18. LPC is the market leader in 50 products and amongst top 3 in 107 of its marketed products.

Company has received 231 approvals till date and has 33 FTF filings including 16 exclusive FTF. Going forward, LPC expects to launch 20-30 generic products in FY18E.

India business – (~27% of sales)

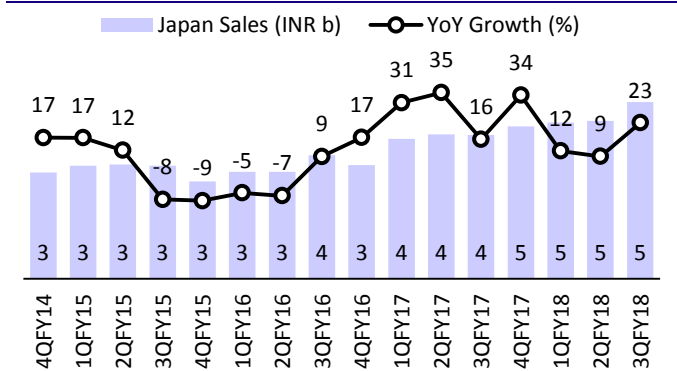
- In 3Q, domestic business posted growth of ~8% YoY, but declined ~18% QoQ.
- During the quarter, LPC’s prescription business grew by ~41%.

Exhibit 5: Domestic business grew 8% YoY



Source: Company, MOSL

Exhibit 6: Japan sales grew significantly by 23% YoY



Source: Company, MOSL

Goa and Indore key plants for LPC; early resolution critical:

Out of 158 pending ANDAs, ~40-50 are from the Goa and Indore facilities. Out of these, ~20-25 approvals were expected in next 12- 18 months. LPC is planning to initiate site transfer for ~12 key ANDAs. Though Tamiflu and Levothyroxine approval will not get impacted due to this, key approvals including Ranexa, Toprol XL, Sevelamer and few other ER products will get stuck. We also expect margins to come under pressure due to negative operating leverage and remediation cost related to retrospective studies and consultant cost. LPC does not expect any supply disruption due to issuance of WL.

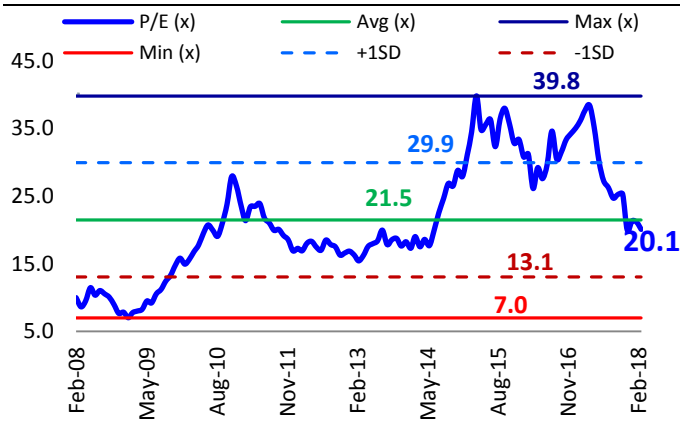
Highlights from Con call

- LPC believes that price erosion in the US business has bottomed out and will be in single-digit for next few quarters.
- Although US base business will face certain price erosion, company expects that it will be offset by new product launches.
- LPC has guided for 10 products to be launched in 4QFY18, including Tamiflu and Axiron and Solosec in 1QFY19E.
- Company plans to launch Levothyroxine by mid-2018.
- On Hydrocodone APAP, company expects pick-up from 4Q, and expects ~15% market share.
- LPC has already started remediation process of Goa and Pithampur plants, and expect it to finish by April-May.
- Albuterol, filed by LPC in Jan17, is being reviewed by the US FDA; it expects approval by 2018/early 2019 and launch by 2019.

Valuation and view

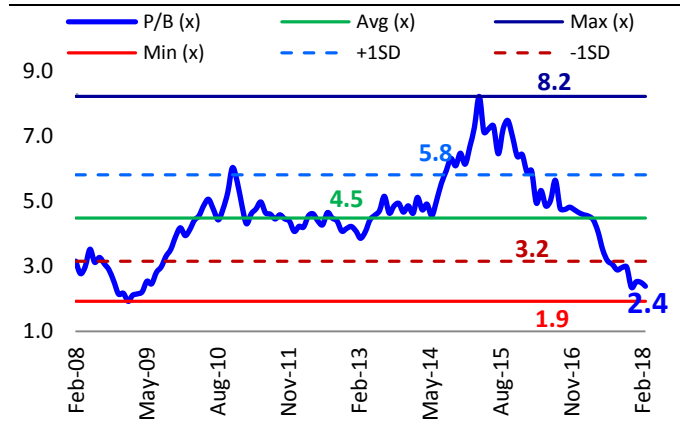
LPC has invested ~INR60b toward R&D over FY16-18E (much higher than what it invested in a decade prior to that). GMP compliance is key to monetize this investment. Although the stock faces near-term pressure, key approvals in the US and resolution of the WL status (expected in 12 months) will help create value in 12-18 months. We maintain Buy with a TP of INR940 @ 20x 1HFY20E PER (v/s INR1,000 @20x 1HFY20E PER). We cut FY18E and FY19/20E EPS by ~6% and 5%, respectively, as we build in the cost impact.

Exhibit 7: P/E valuation band (10 years)



Source: Company, MOSL

Exhibit 8: Higher premium relative to Sensex



Source: Company, MOSL

Operating metrics

Exhibit 9: Key operating metrics

	2QFY15	3QFY15	4QFY15	1QFY16	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18
Revenue Mix (%)														
US	40.8	44.7	45.1	38.7	36.1	41.8	53.5	50.4	47.4	49.4	45.7	42.1	35.1	36.7
India	25.6	23.7	21.7	28.8	27.8	25.9	18.6	21.9	23.6	22.5	21.1	24.5	29.9	27.4
Japan	11.1	10.9	9.6	10.5	10.1	11.1	8.4	9.7	10.4	9.9	11.1	12.4	12.3	13.7
Europe	2.8	2.6	2.9	2.8	3.8	3.0	3.1	2.9	2.6	3.2	3.8	3.4	3.9	3.5
ROW	9.4	9.5	10.5	8.6	11.7	9.8	9.5	8.2	9.0	9.0	11.6	10.3	11.9	11.8
APIs	10.2	8.8	10.1	10.6	10.4	8.2	6.9	6.8	6.9	6.1	6.8	7.3	6.8	6.9
Revenue Growth (%)														
US	18.4	5.4	0.1	(6.4)	2.4	6.8	34.0	41.2	31.9	30.5	1.2	(12.8)	(8.5)	(11.5)
India	22.9	3.5	(6.3)	(25.8)	(9.3)	0.0	58.7	83.8	73.1	54.9	(13.1)	(26.8)	(31.9)	(34.2)
Japan	20.4	14.4	15.2	16.2	11.2	17.1	14.7	7.3	12.1	13.8	15.4	(1.8)	16.4	7.8
Europe	11.8	(8.0)	(8.5)	(5.4)	(6.5)	9.3	17.0	31.0	35.1	16.2	34.0	11.6	9.4	22.9
ROW	18.2	21.8	12.1	24.1	39.3	25.5	40.7	49.5	(8.6)	39.3	26.1	0.6	34.7	(3.6)
APIs	11.7	24.0	2.8	23.5	26.4	10.9	21.1	34.6	1.4	19.3	23.7	10.3	22.1	17.1
APIs	11.2	(7.2)	5.5	11.4	4.6	0.1	(7.7)	(8.9)	(12.3)	(2.8)	(0.8)	(5.8)	(9.2)	(0.1)
Expense as % of sales														
Raw material	75.1	73.0	74.9	75.7	83.5	79.8	70.2	72.8	77.5	74.2	75.6	75.2	80.0	84.3
Staff cost	34.3	32.5	31.3	31.9	35.2	33.4	27.0	29.3	29.5	29.5	28.5	28.9	33.2	35.7
Staff cost	14.1	13.2	15.8	16.1	16.7	15.7	14.2	16.3	16.9	16.6	17.0	16.5	18.7	17.8
R&D cost	9.1	8.3	10.1	10.2	12.1	11.7	12.5	11.5	13.6	12.9	16.1	13.4	12.2	12.2
Other expenses	17.6	18.9	17.7	17.4	19.5	18.9	16.5	15.7	17.5	15.1	14.0	16.4	15.8	18.6
Tax Rate	23.1	28.0	19.5	28.5	27.4	35.4	35.8	23.7	19.4	39.3	26.4	27.7	26.5	42.0
Margins (%)														
Gross Margins	65.7	67.5	68.7	68.1	64.8	66.6	73.0	70.7	70.5	70.5	71.5	71.1	66.8	64.3
EBITDA Margins	26.2	27.8	25.6	26.1	19.9	24.7	31.3	29.3	24.0	27.1	26.0	25.7	21.6	17.3
EBIT Margins	24.0	27.2	22.9	25.9	18.9	24.8	29.2	27.4	20.0	24.7	21.2	21.3	16.9	11.2
PAT margins	20.2	19.1	17.9	18.5	13.1	15.8	18.3	20.3	15.7	14.4	9.1	14.8	11.7	5.7

Source: Company; MOSL

Story in charts

Exhibit 10: Revenue mix in 3QFY18

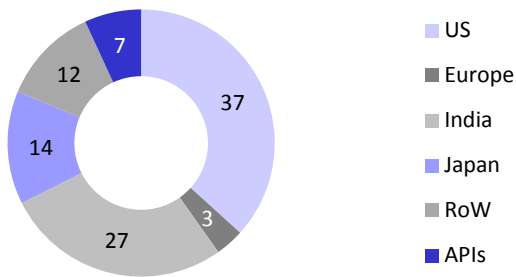


Exhibit 11: Growth to slow down due to regulatory issues

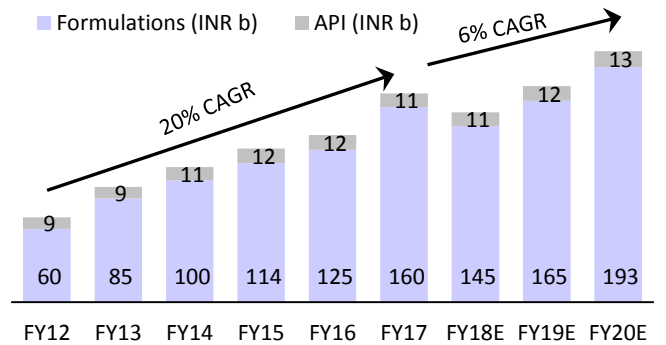


Exhibit 12: R&D expense to be in the range of 12-13%

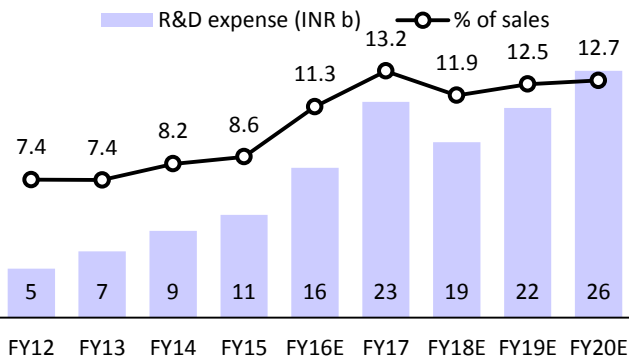


Exhibit 13: Margins to gradually pick up

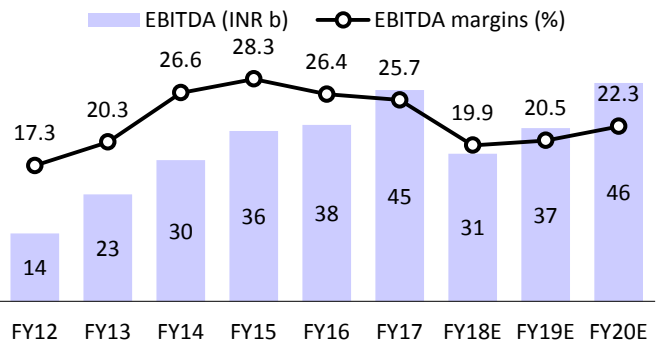


Exhibit 14: EPS to improve FY18 onwards

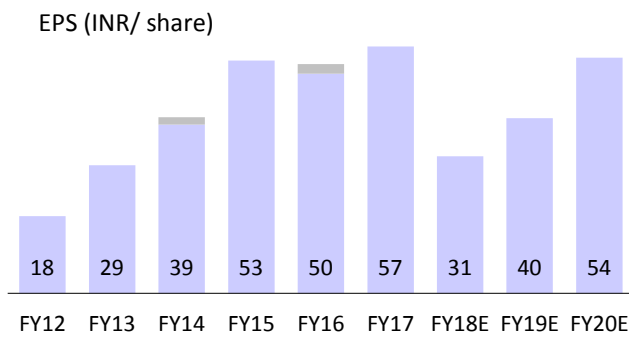
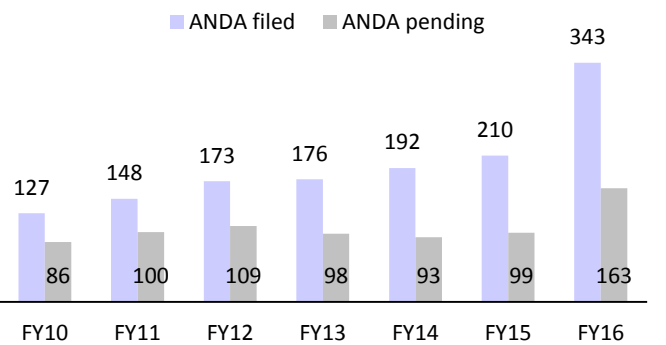


Exhibit 15: Rich ANDA pipeline



Financials and Valuations

Income Statement							(INR m)
Y/E March	2014	2015	2016	2017	2018E	2019E	2020E
Net Sales	112,866	127,700	142,085	174,943	157,798	179,608	208,230
Change (%)	17.1	13.1	11.3	23.1	-9.8	13.8	15.9
EBITDA	30,028	36,196	37,534	44,931	31,402	36,820	46,435
Margin (%)	26.6	28.3	26.4	25.7	19.9	20.5	22.3
Depreciation	2,610	4,347	4,635	9,122	10,926	11,475	12,234
EBIT	27,418	31,849	32,899	35,809	20,475	25,345	34,201
Int. and Finance Charges	267	98	446	1,525	1,984	2,026	2,111
Other Income - Rec.	165	2,398	1,877	1,065	1,650	1,500	1,500
PBT before EO item	27,317	34,148	34,330	35,349	20,141	24,818	33,590
EO Expense/(Income)	-1,000	0	0	0	0	0	0
PBT after EO item	28,317	34,148	34,330	35,349	20,141	24,818	33,590
Tax	9,622	9,704	11,536	9,785	5,841	6,577	9,069
Tax Rate (%)	34.0	28.4	33.6	27.7	29.0	26.5	27.0
Less: Minority Interest	331	412	88	-11	85	85	85
Reported PAT	18,364	24,032	22,707	25,574	14,215	18,157	24,436
PAT Adj for EO items	17,364	24,032	22,707	25,574	14,215	18,157	24,436
Change (%)	32.1	38.4	-5.5	12.6	-44.4	27.7	34.6
Margin (%)	15.4	18.8	16.0	14.6	9.0	10.1	11.7

Consolidated Balance Sheet							(INR m)
Y/E March	2014	2015	2016	2017	2018E	2019E	2020E
Equity Share Capital	897	899	901	903	903	903	903
Total Reserves	68,419	87,842	108,943	134,072	143,532	156,934	176,615
Net Worth	69,316	88,741	109,844	134,975	144,436	157,837	177,518
Minority Interest	669	241	321	345	430	515	600
Deferred liabilities	1,779	1,182	1,239	-1,128	-1,128	-1,128	-1,128
Secured Loan	1,968	1,018	53,739	61,243	61,243	61,243	61,243
Unsecured Loan	4,024	3,692	17,454	23,183	23,183	23,183	23,183
Total Loans	5,992	4,710	71,193	84,426	84,426	84,426	84,426
Capital Employed	77,756	94,874	182,596	218,619	228,164	241,651	261,416
Gross Block	45,638	45,445	55,887	55,265	68,285	81,192	94,043
Less: Accum. Deprn.	19,283	19,174	23,262	8,902	24,550	36,025	48,259
Net Fixed Assets	26,355	26,271	32,625	46,363	43,734	45,167	45,784
Capital WIP	3,041	5,760	9,812	7,150	6,925	6,812	6,756
Investments	1,785	16,584	75	220	220	220	220
Goodwill & Intangibles	7,202	17,411	73,586	78,147	82,869	82,869	82,869
Curr. Assets	62,970	64,510	107,473	129,117	136,558	151,966	176,261
Inventory	21,295	25,036	31,787	36,423	30,463	33,833	38,981
Account Receivables	24,641	26,566	45,498	43,073	41,305	47,014	54,506
Cash and Bank Balance	7,975	4,814	8,379	27,994	43,049	49,253	60,768
Others	9,060	8,095	21,808	21,626	21,741	21,867	22,006
Curr. Liability & Prov.	23,597	35,662	40,975	42,378	42,142	45,384	50,473
Account Payables	18,818	28,299	32,318	34,576	29,908	33,076	37,916
Provisions	4,779	7,363	8,658	7,801	12,234	12,308	12,557
Net Current Assets	39,374	28,848	66,498	86,739	94,416	106,582	125,788
Appl. of Funds	77,756	94,874	182,596	218,619	228,164	241,651	261,417

E: MOSL Estimates

Financials and Valuations

Ratios

Y/E March	2014	2015	2016	2017	2018E	2019E	2020E
EPS (Fully Diluted)	38.7	53.5	50.4	56.6	31.5	40.2	54.1
Cash EPS (Fully Diluted)	44.5	63.1	60.7	76.8	55.7	65.6	81.2
BV/Share	154.6	197.4	243.8	298.9	319.8	349.5	393.1
DPS	6.0	7.5	7.5	9.0	9.0	9.0	9.0
Payout (%)	16.0	16.9	17.9	18.6	33.5	26.2	19.5

Valuation (x)

P/E (Fully Diluted)	20.7	15.0	15.9	14.2	25.5	19.9	14.8
Cash P/E (Fully Diluted)	18.0	12.7	13.2	10.4	14.4	12.2	9.9
P/BV	5.2	4.1	3.3	2.7	2.5	2.3	2.0
EV/Sales	3.5	3.1	3.2	2.6	2.8	2.4	2.0
EV/EBITDA	13.1	11.0	12.2	10.1	13.9	11.7	9.0

Return Ratios (%)

RoE	28.6	30.4	22.9	20.9	10.2	12.0	14.6
RoCE	26.5	29.1	16.8	13.3	7.0	8.4	10.3
RoIC	29.7	34.4	18.8	14.9	8.0	10.3	13.2

Leverage Ratio

Current Ratio	2.7	1.8	2.6	3.0	3.2	3.3	3.5
Interest Cover Ratio	102.9	324.7	73.7	23.5	10.3	12.5	16.2
Debt/Equity (x)	0.1	0.1	0.7	0.6	0.6	0.5	0.5

Cash Flow Statement

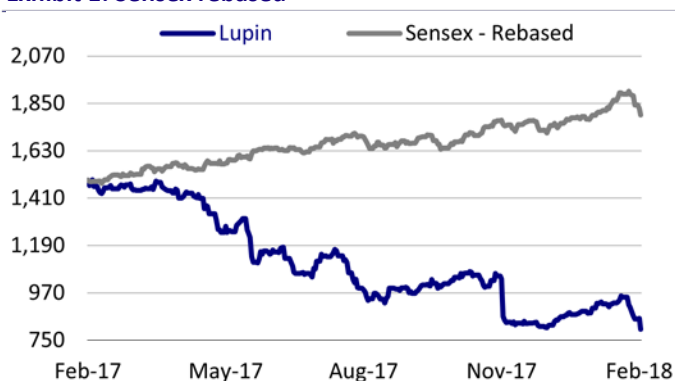
Y/E March	2014	2015	2016	2017	2018E	2019E	2020E
Oper. Profit before Tax	30,028	36,196	37,534	44,931	31,402	36,820	46,435
Interest/Dividends Recd.	165	2,398	1,877	1,065	1,650	1,500	1,500
Direct Taxes Paid	-9,475	-10,300	-11,479	-12,152	-5,841	-6,577	-9,069
(Inc)/Dec in WC	-4,368	7,364	-34,084	-626	7,378	-5,963	-7,690
CF from Op. incl EO Exp.	17,349	35,657	-6,152	33,219	34,589	25,780	31,176
(inc)/dec in FA	-6,098	-17,191	-71,217	-24,759	-12,795	-12,795	-12,795
Free Cash Flow	10,251	18,466	-77,369	8,460	21,794	12,985	18,381
(Pur)/Sale of Investments	-1,764	-14,799	16,509	-145	0	0	0
CF from Investments	-7,862	-31,991	-54,708	-24,904	-12,795	-12,795	-12,795
Change in Net Worth	1,593	-1,389	2,459	4,348	0	0	0
Inc/(Dec) in Debt	-4,248	-1,282	66,483	13,233	0	0	0
Interest Paid	-267	-98	-446	-1,525	-1,984	-2,026	-2,111
Dividend Paid	-2,939	-4,058	-4,071	-4,755	-4,755	-4,755	-4,755
CF from Fin. Activity	-5,861	-6,828	64,425	11,300	-6,739	-6,781	-6,866
Inc/Dec of Cash	3,626	-3,161	3,565	19,615	15,055	6,203	11,516
Add: Beginning Balance	4,349	7,975	4,814	8,379	27,994	43,049	49,253
Closing Balance	7,975	4,814	8,379	27,994	43,049	49,253	60,768

Corporate profile

Company description

Lupin is amongst the larger pharma companies that is actively targeting the regulated generics markets. Historically very strong in the anti-TB segment, it has over the years built up expertise in fermentation-based products and segments like cephalosporins, prils and statins. Lupin is now a fully integrated company, with manufacturing capabilities in APIs and formulations and a direct marketing presence in the target markets.

Exhibit 1: Sensex rebased



Source: MOSL/Bloomberg

Exhibit 2: Shareholding pattern (%)

	Dec-17	Sep-17	Dec-16
Promoter	47.0	46.8	46.7
DII	12.1	12.4	8.2
FII	25.6	27.7	33.3
Others	15.4	13.1	11.8

Note: FII Includes depository receipts

Source: Capitaline

Exhibit 3: Top holders

Holder Name	% Holding
LIFE INSURANCE CORPORATION OF INDIA	2.7
Rakesh Jhunjhunwala	1.9
ICICI Prudential Mutual Funds	1.4
Government Pension Fund Global	1.2

Source: Capitaline

Exhibit 4: Top management

Name	Designation
D B Gupta	Chairman
Kamal K Sharma	Vice Chairman
Nilesh Gupta	Managing Director
Ramesh Swaminathan	Director & CFO
M D Gupta	Executive Director
R V Satam	Company Secretary
Vinita Gupta	CEO & Director

Source: Capitaline

Exhibit 5: Directors

Name	Name
Dileep C Choksi	Jean-Luc Belingard
K U Mada	R A Shah
Richard Zahn	Vijay Kelkar

*Independent

Exhibit 6: Auditors

Name	Type
B S R & Co LLP	Statutory
Ernst & Young LLP	Internal
Neena Bhatia	Secretarial Audit
Price Waterhouse & Co Bangalore LLP	Internal
S D Shenoy	Cost Auditor

Source: Capitaline

Exhibit 7: MOSL forecast v/s consensus

EPS (INR)	MOSL forecast	Consensus forecast	Variation (%)
FY18	31.5	38.8	-18.8
FY19	40.2	45.5	-11.7
FY20	54.1	54.7	-1.1

Source: Bloomberg

Explanation of Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10% to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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