

BUY

TP: Rs 900 | ▲ 14%

CIPLA

Pharmaceuticals

07 November 2020

Comprehensive Q2 beat; India drives good surprise

Cipla reported a Q2 sales/EBITDA beat of 13%/17% led by (1) outperformance in India (Covid portfolio contributed ~5% sales/EBITDA) and CGA sales, and (2) cost control (-13% YoY). Excluding one-offs in trade generics, the EBITDA beat was still healthy at 10%. Margins were solid at 23.4% (22% ex-Albuterol). Steady cost optimisation and ROI improvement remain priorities. Albuterol ramp-up, Advair approval and a strong India franchise are key stock catalysts. We raise FY22-FY23 EPS by 7-13% and our Sep'21 TP to Rs 900 (vs. Rs 850).

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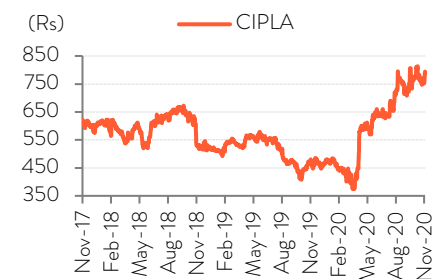
All-round sales beat led by India; US in line: India sales grew 20% YoY (branded +14% YoY boosted by Covid portfolio). Trade generics saw bunching up in Q2 and hence should moderate. Consumerisation product trends continue to gain pace from the trade generics to OTC switch (contributed ~5% of sales). The Covid portfolio formed ~5% of sales – of this, ~30% is sustainable, per Cipla. US sales were led by Albuterol (~US\$ 20mn). Cipla has clocked 84% of prescription share in Proventil (Proventil market share up to 10% from 6%). CGA tender sales grew 65% QoQ on a robust order book, EU 30% YoY and API 20% on a low base.

Ticker/Price	CIPLA IN/Rs 790
Market cap	US\$ 8.6bn
Shares o/s	806mn
3M ADV	US\$ 90.9mn
52wk high/low	Rs 829/Rs 355
Promoter/FPI/DII	37%/26%/13%

Source: NSE

Margin beat; tracking ahead on targeted FY21 cost savings: Adj. EBITDA margin came in ahead of estimates at 22% led by (1) lower SGA (-13% YoY) due to cost optimisation, and (2) lower R&D-to-sales of 4.5% (could rise to 6% by Q4 on incremental Advair trials). Cipla is tracking ahead of the targeted Rs 4bn-5bn of cost savings from digital initiatives in FY21 and a majority of these savings are expected to continue at least for the next two years.

STOCK PERFORMANCE



Earnings call takeaways: (1) US business margins trending close to company level in H1. (2) Albuterol: Cipla clocked 8% share of weekly Rx across brands. Share gains to be gradual; pricing stable. (3) Net cash at Rs 4.5bn (vs. net debt of Rs 8.1bn in Mar'20). (4) Remdesivir supplies commenced for multiple EMs.

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	163,621	171,243	186,103	198,465	213,811
EBITDA (Rs mn)	30,973	32,574	40,824	42,938	44,812
Adj. net profit (Rs mn)	13,426	15,858	22,122	23,200	24,864
Adj. EPS (Rs)	16.7	19.7	27.5	28.8	30.9
Adj. EPS growth (%)	8.8	18.1	39.5	4.9	7.2
Adj. ROAE (%)	9.0	10.0	12.6	11.8	11.4
Adj. P/E (x)	47.4	40.1	28.8	27.4	25.6
EV/EBITDA (x)	21.3	20.1	15.7	14.6	13.6

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Q2FY21E	Var. (%)	H1FY21	H1FY20	YoY (%)
Net Sales	50,383	43,957	14.6	43,461	15.9	44,412	13.4	93,844	83,846	11.9
EBITDA	11,765	9,096	29.3	10,490	12.2	10,063	16.9	22,255	18,143	22.7
Depreciation	2,651	2,829	-	2,689	-	2,829	-	5,340	5,509	-
EBIT	9,114	6,267	45.4	7,801	16.8	7,234	-	16,915	12,634	-
Interest	393	460	-	460	-	460	-	853	981	-
Other Income	535	1,005	-	654	-	1,005	-	1,189	1,788	-
PBT	9,256	6,812	35.9	7,995	15.8	7,779	19.0	17,251	13,441	28.3
Less: Taxation	2,638	2,005	-	2,277	-	2,005	-	4,915	3,927	-
Less: Minority Interest	(35)	90	-	(64)	-	90	-	(99)	15	-
Recurring PAT	6,653	4,717	41.0	5,782	15.1	5,684	17.0	12,435	9,499	30.9
Exceptional Items	0	0	-	0	-	0	-	0	0	-
Reported PAT	6,653	4,717	41.0	5,782	15.1	5,684	17.0	12,435	9,499	30.9
Key Ratios (%)										
Gross Margin	61.4	66.8	-	63.4	-	63.5	-	62.3	68.3	-
EBITDA Margin	23.4	20.7	-	24.1	-	22.7	-	23.7	21.6	-
Tax / PBT	28.5	29.4	-	28.5	-	25.8	-	28.5	29.2	-
NPM	13.2	10.7	-	13.3	-	12.8	-	13.3	11.3	-
EPS (Rs)	8.3	5.9	-	7.2	-	7.1	-	15.5	11.8	-

Source: Company, BOBCAPS Research

FIG 2 – REVENUE MIX

(Rs mn)	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	Q2FY21E	Var. (%)	H1FY21	H1FY20	YoY (%)
Formulations	47,840	40,790	17.3	40,890	17.0	41,985	13.9	88,730	77,240	14.9
India	20,900	17,450	19.8	16,080	30.0	18,170	15.0	36,980	31,000	19.3
US	10,490	9,530	10.1	10,210	2.7	10,360	1.3	20,700	20,720	(0.1)
SAGA	9,240	7,400	24.9	7,630	21.1	7,327	26.1	16,870	14,310	17.9
South Africa	5,690	5,460	4.2	5,480	3.8	5,353	6.3	11,170	10,780	3.6
Others/Global Access	3,550	1,940	83.0	2,150	65.1	1,974	79.9	5,700	3,530	61.5
Europe	2,470	1,900	30.0	2,400	2.9	2,128	16.1	4,870	3,910	24.6
ROW	4,740	4,510	5.1	4,570	3.7	4,000	18.5	9,310	7,300	27.5
APIs	1,890	1,570	20.4	1,840	2.7	1,696	11.5	3,730	3,390	10.0
Other Op. income	653	1,590	(58.9)	731	(10.7)	731	(10.7)	1,384	3,190	(56.6)
Net Sales	50,383	43,950	14.6	43,461	15.9	44,412	13.4	93,844	83,820	12.0
INR/US\$	74	70	5.0	75	(2.0)	74	-	74	70	6.1
US in \$ terms	143	136	4.8	136	4.8	141	-	279	296	(5.8)

Source: Company, BOBCAPS Research

Valuation methodology

We like Cipla for its strong India franchise, rich US pipeline and low risk of price erosion in the US market (top 3 products form 25% of US sales). Operating leverage in the US business would be a key margin driver in the next two years. We believe Cipla’s future investments will have a sharper focus on opportunities in high-value/complex assets, but not at the expense of current margins.

We increase our FY22-FY23 EPS estimates by 7-13% and continue to expect a core EPS CAGR of 15% over FY20-FY23. Advair approval represents an upside risk to our EPS estimates. We retain BUY and raise our Sep’21 target price to Rs 900 (from Rs 850), based on an unchanged 16x EV/EBITDA multiple and implied P/E of 31x. Our target valuation multiple is at the midpoint of the eight-year historical band (11-21x) and 15% higher than frontline stocks (Sun Pharma, Lupin, Dr Reddy’s) due to Cipla’s higher branded product share in EBITDA (>70%).

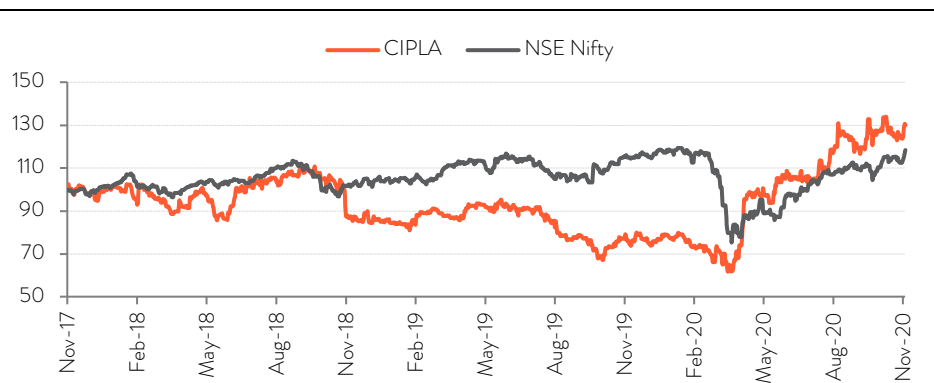
We see scope for further stock rerating on the back of (1) margin upside potential accruing from higher operating leverage as the company’s ‘One India’ strategy gains momentum and cost optimisation remains in focus, and (2) ROIC closing in on peak levels of 20% in the next two years. The global generic environment, especially in the US, remains supportive.

FIG 3 – REVISED ESTIMATES

(Rs bn)	New			Old			Change (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Sales	186.1	198.5	213.8	178.1	191.9	207.4	4.5	3.4	3.1
EBITDA	40.8	42.9	44.8	35.1	39.0	42.7	16.4	10.1	4.9
EBITDA margin (%)	21.9	21.6	21.0	19.7	20.3	20.6	225bps	131bps	36bps
EPS (Rs)	27	29	31	22	25.4	29	23.5	13.4	6.6

Source: Company, BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

- **US execution critical:** We expect the US market to contribute meaningfully to profitability in the coming years. Any delay in ramp up of key launches like Proventil HFA and Flonase can potentially erode 4-5% of FY21E EPS.
- **Reduction in Global Access funding:** A decline in the tender-facing Global Access business due to challenges in the funding environment would pose a risk to our estimates.
- **Weak drug price hikes in South Africa.**

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	163,621	171,243	186,103	198,465	213,811
EBITDA	30,973	32,574	40,824	42,938	44,812
Depreciation	13,263	11,760	12,893	13,924	15,038
EBIT	17,710	20,814	27,931	29,014	29,774
Net interest income/(expenses)	(1,684)	(1,972)	(1,144)	(715)	(447)
Other income/(expenses)	2,915	3,331	3,517	3,482	4,733
Exceptional items	0	0	0	0	0
EBT	18,941	22,173	30,304	31,781	34,061
Income taxes	5,696	6,310	8,182	8,581	9,196
Extraordinary items	1,850	0	0	0	0
Min. int./Inc. from associates	(181)	5	0	0	0
Reported net profit	15,277	15,858	22,122	23,200	24,864
Adjustments	1,850	0	0	0	0
Adjusted net profit	13,426	15,858	22,122	23,200	24,864

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	19,480	25,013	24,808	26,704	28,801
Other current liabilities	10,126	9,960	10,866	11,696	12,615
Provisions	8,582	8,919	9,731	10,474	11,297
Debt funds	43,161	28,160	17,600	11,000	6,875
Other liabilities	0	0	0	0	0
Equity capital	1,611	1,613	1,613	1,613	1,613
Reserves & surplus	154,016	167,461	187,163	207,944	230,390
Shareholders' fund	155,627	169,073	188,776	209,557	232,002
Total liabilities and equities	236,976	241,125	251,781	269,431	291,591
Cash and cash eq.	6,188	9,630	13,148	27,054	42,262
Accounts receivables	41,507	38,910	39,693	40,055	43,202
Inventories	39,648	43,204	49,616	53,407	57,602
Other current assets	21,866	23,239	25,354	27,291	29,435
Investments	25,539	25,539	25,539	25,539	25,539
Net fixed assets	51,144	48,053	46,967	45,794	44,527
CWIP	6,762	8,245	8,245	8,245	8,245
Intangible assets	44,322	44,305	43,219	42,046	40,779
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	236,975	241,125	251,781	269,431	291,591

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	28,540	27,618	35,014	37,124	39,902
Interest expenses	1,684	1,972	1,144	715	447
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(6,412)	3,373	(7,797)	(2,621)	(5,646)
Other operating cash flows	0	0	0	0	0
Cash flow from operations	23,812	32,963	28,362	35,218	34,703
Capital expenditures	(6,228)	(10,932)	(11,807)	(12,751)	(13,771)
Change in investments	(12,953)	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(19,181)	(10,932)	(11,807)	(12,751)	(13,771)
Equities issued/Others	1	1	0	0	0
Debt raised/repaid	2,181	(15,001)	(10,560)	(6,600)	(4,125)
Interest expenses	(1,684)	(1,972)	(1,144)	(715)	(447)
Dividends paid	(2,417)	(2,419)	(2,419)	(2,419)	(2,419)
Other financing cash flows	(6,181)	801	1,086	1,173	1,267
Cash flow from financing	(8,099)	(18,590)	(13,037)	(8,561)	(5,724)
Changes in cash and cash eq.	(3,468)	3,441	3,519	13,906	15,208
Closing cash and cash eq.	6,187	9,629	13,148	27,054	42,262

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	19.0	19.7	27.5	28.8	30.9
Adjusted EPS	16.7	19.7	27.5	28.8	30.9
Dividend per share	3.0	3.0	3.0	3.0	3.0
Book value per share	188.9	205.6	230.0	255.8	283.6

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	4.0	3.8	3.5	3.2	2.9
EV/EBITDA	21.3	20.1	15.7	14.6	13.6
Adjusted P/E	47.4	40.1	28.8	27.4	25.6
P/BV	4.2	3.8	3.4	3.1	2.8

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	70.9	71.5	73.0	73.0	73.0
Interest burden (PBT/EBIT)	107.0	106.5	108.5	109.5	114.4
EBIT margin (EBIT/Revenue)	10.8	12.2	15.0	14.6	13.9
Asset turnover (Revenue/Avg TA)	21.0	21.6	23.1	23.2	23.3
Leverage (Avg TA/Avg Equity)	1.3	1.2	1.1	1.1	1.1
Adjusted ROAE	9.0	10.0	12.6	11.8	11.4

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	7.5	4.7	8.7	6.6	7.7
EBITDA	9.6	5.2	25.3	5.2	4.4
Adjusted EPS	8.8	18.1	39.5	4.9	7.2
Profitability & Return ratios (%)					
EBITDA margin	18.9	19.0	21.9	21.6	21.0
EBIT margin	10.8	12.2	15.0	14.6	13.9
Adjusted profit margin	8.2	9.3	11.9	11.7	11.6
Adjusted ROAE	9.0	10.0	12.6	11.8	11.4
ROCE	10.6	12.2	15.6	15.2	15.0
Working capital days (days)					
Receivables	95	86	80	75	75
Inventory	91	95	100	100	100
Payables	45	55	50	50	50
Ratios (x)					
Gross asset turnover	1.2	1.2	1.2	1.2	1.2
Current ratio	2.9	2.6	2.8	3.0	3.3
Net interest coverage ratio	10.5	10.6	24.4	40.6	66.6
Adjusted debt/equity	0.1	0.0	(0.1)	(0.2)	(0.2)

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

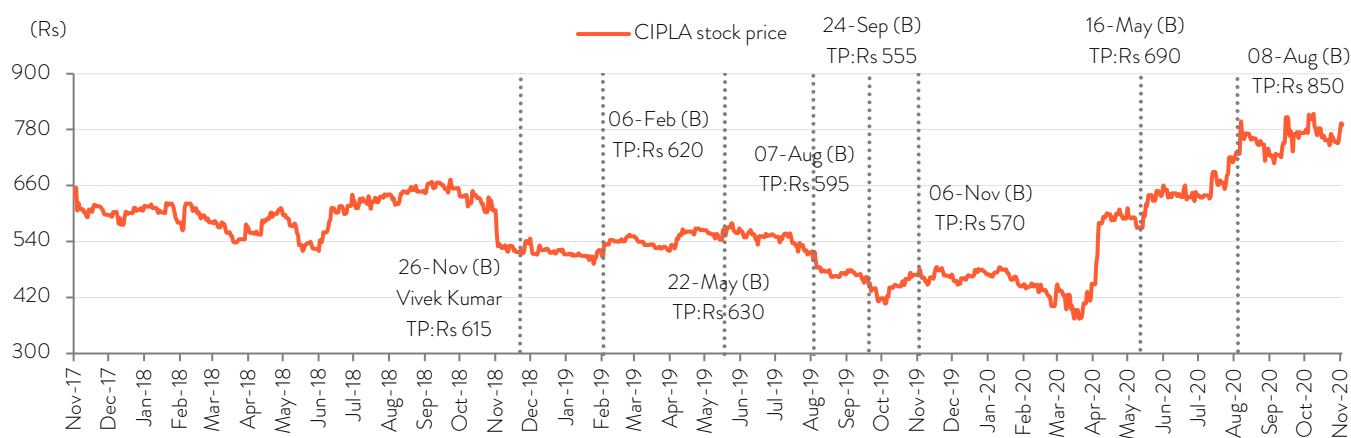
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): CIPLA (CIPLA IN)



B – Buy, A – Add, R – Reduce, S – Sell

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