

**BUY**

TP: Rs 1,160 | ▲ 28%

**CIPLA**

| Pharmaceuticals

| 27 October 2021

## Results better than expected; EBITDA margin resilient

- Q2 revenue/EBITDA grew 10%/4% YoY to Rs 55bn/Rs 12bn, beating our estimates by 6%/4%
- Cost control and a better mix kept EBITDA margin healthy at 22.2% despite lower Covid product contribution and US price erosion
- Launch momentum to continue with a high-value pipeline for H2FY23. Reiterate BUY; TP unchanged at Rs 1,160

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**Highest quarterly revenue:** Cipla reported its highest-ever quarterly revenue of Rs 55.2bn (+10% YoY) in Q2FY22 on the back of 11% growth in formulations while API revenue declined 9% YoY. India business grew 16% YoY (-11% QoQ) on a high base led by sustained volume traction across core therapies, even though Covid portfolio contribution moderated.

**Branded formulations perform well:** International revenue grew 14% YoY, supported by resumption of Middle Eastern supplies, strong performance in direct-to-market (DTM) businesses, and contribution from Covid products. The company continued to grow ahead of the market in South Africa private business (+40% YoY USD), while SAGA growth was muted at 7% YoY USD as SSA-CGA declined 21% due to order confirmation delays by some clients and an 8% decline in SA tender business.

**US launch momentum to continue:** US business was steady at US\$ 142mn (+1% YoY/QoQ) due to continued momentum in core products (Diclofenac, Citalopram, Omeprazole), offsetting price erosion in the rest of the portfolio. Cipla reported generic prescription market share of 18%/39% for Albuterol/ Arformoterol for the week ended 8 October. It continues to focus on limited-competition, complex launches and has products such as Revlimid, Abraxane and Advair in the pipeline.

**Prudent cost control; targeting FY22 margin of 22%:** Gross margin contracted 100bps QoQ in Q2 due to lower Covid portfolio contribution and non-recurring inventory provisions. Higher R&D spend at 5% of revenue (vs. 4.5% same period last year) and resumption of offline promotional activities resulted in EBITDA margin falling 115bps YoY to 22.2% (-225bps QoQ). Margin stress was partly offset by prudent cost controls, but input cost escalation from China could strain margins near term.

**Reiterate BUY:** We like Cipla for its strong India franchise, rich US pipeline and low risk of price erosion in the US market. We thus retain BUY and keep our Sep'22 TP at Rs 1,160, based on an unchanged 17x forward EV/EBITDA multiple (implied P/E of 28x). Our target multiple is at the midpoint of the stock's 10-year historical band (12-22x) and 8% lower than that for Sun Pharma.

## Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	CIPLA IN/Rs 908
Market cap	US\$ 9.8bn
Free float	63%
3M ADV	US\$ 33.1mn
52wk high/low	Rs 1,005/Rs 707
Promoter/FPI/DII	36%/25%/21%

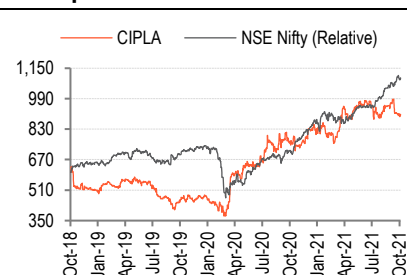
Source: NSE | Price as of 26 Oct 2021

## Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	1,91,595	2,16,263	2,35,667
EBITDA (Rs mn)	42,524	47,567	50,362
Adj. net profit (Rs mn)	24,048	27,604	29,733
Adj. EPS (Rs)	29.8	34.3	36.9
Consensus EPS (Rs)	29.8	35.1	41.7
Adj. ROAE (%)	14.1	14.2	13.5
Adj. P/E (x)	30.4	26.5	24.6
EV/EBITDA (x)	17.5	15.2	14.0
Adj. EPS growth (%)	55.6	14.8	7.7

Source: Company, Bloomberg, BOBCAPS Research

## Stock performance



Source: NSE



## Earnings call highlights

- Cipla indicated that it is on track for Goa plant remediation and in constant communication with the USFDA. The Goa plant is critical for gAbraxane.
- Communications are ongoing with the USFDA with regards to both gAdvair and gAbraxane. The company has responded to the regulator on the gAdvair CRL.
- Cipla launched biosimilar Bevacizumab during the quarter in partnership with mAbxience in Spain which has strengthened its oncology portfolio.
- Overall US price erosion in Q2FY22 was in the mid-single digits, in line with historical trends.
- The recent JV with Kemwell will leverage Cipla and Kemwell's complementary strengths for end-to-end product development, clinical development, regulatory filings, manufacturing and commercialisation of biopharmaceutical products.
- FY22 capex is planned at Rs 8bn-9bn.

**Fig 1 – Quarterly performance**

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	Q2FY22E	Var (%)	H1FY22	H1FY21	YoY (%)
<b>Net Sales</b>	<b>55,198</b>	<b>50,383</b>	<b>9.6</b>	<b>55,044</b>	<b>0.3</b>	<b>52,123</b>	<b>5.9</b>	<b>1,10,242</b>	<b>93,845</b>	<b>17.5</b>
<b>EBITDA</b>	<b>12,262</b>	<b>11,765</b>	<b>4.2</b>	<b>13,459</b>	<b>(8.9)</b>	<b>11,757</b>	<b>4.3</b>	<b>25,721</b>	<b>22,252</b>	<b>15.6</b>
Depreciation	2,531	2,651	-	2,611	-	-	-	5,142	5,340	-
<b>EBIT</b>	<b>9,731</b>	<b>9,114</b>	<b>6.8</b>	<b>10,848</b>	<b>(10.3)</b>	<b>-</b>	<b>-</b>	<b>20,579</b>	<b>16,912</b>	<b>-</b>
Interest	380	393	-	296	-	-	-	676	853	-
Other Income	607	535	-	649	-	-	-	1,256	1,189	-
<b>PBT</b>	<b>9,958</b>	<b>9,256</b>	<b>7.6</b>	<b>11,201</b>	<b>(11.1)</b>	<b>-</b>	<b>-</b>	<b>21,160</b>	<b>17,248</b>	<b>22.7</b>
Less: Taxation	2,838	2,638	-	2,837	-	-	-	5,675	4,916	-
Less: Minority Interest	6	(35)	-	(29)	-	-	-	(23)	(100)	-
<b>Recurring PAT</b>	<b>7,114</b>	<b>6,653</b>	<b>6.9</b>	<b>8,393</b>	<b>(15.2)</b>	<b>6,989</b>	<b>1.8</b>	<b>15,507</b>	<b>12,432</b>	<b>24.7</b>
Exceptional items	0	0	-	(1,246)	-	-	-	(1,246)	0	-
<b>Reported PAT</b>	<b>7,114</b>	<b>6,653</b>	<b>6.9</b>	<b>7,147</b>	<b>(0.5)</b>	<b>-</b>	<b>-</b>	<b>14,261</b>	<b>12,432</b>	<b>14.7</b>
<b>Key Ratios (%)</b>			<b>(bps)</b>		<b>(bps)</b>					<b>(bps)</b>
Gross Margin	61.3	61.4	(7)	62.4	(112)	-	-	61.9	62.3	-
EBITDA Margin	22.2	23.4	(114)	24.5	(224)	22.6	(34)	23.3	23.7	-
Tax / PBT	28.5	28.5	-	25.3	-	-	-	26.8	28.5	-
NPM	12.9	13.2	(32)	15.2	(236)	13.4	(52)	14.1	13.2	-
<b>EPS (Rs)</b>	<b>8.8</b>	<b>8.3</b>	<b>-</b>	<b>10.4</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>19.2</b>	<b>15.4</b>	<b>-</b>

Source: Company, BOBCAPS Research

**Fig 2 – Revenue mix**

(Rs mn)	Q2FY22	Q2FY21	YoY (%)	Q1FY22	QoQ (%)	H1FY22	H1FY21	YoY (%)
<b>Formulations</b>	<b>52,860</b>	<b>47,700</b>	<b>10.8</b>	<b>51,670</b>	<b>2.3</b>	<b>1,04,530</b>	<b>88,590</b>	<b>18.0</b>
India	24,160	20,900	15.6	27,100	(10.8)	51,260	36,980	38.6
North America	10,550	10,350	1.9	10,380	1.6	20,930	20,560	1.8
SAGA	9,940	9,230	7.7	8,370	18.8	18,310	16,860	8.6
South Africa	7,100	5,680	25.0	6,340	12.0	13,440	11,160	20.4
Others/Global Access	2,840	3,550	(20.0)	2,030	39.9	4,870	5,700	(14.6)
International	8,210	7,220	13.7	5,820	41.1	14,030	14,190	(1.1)
<b>APIs</b>	<b>1,720</b>	<b>1,890</b>	<b>(9.0)</b>	<b>3,020</b>	<b>(43.0)</b>	<b>4,740</b>	<b>3,730</b>	<b>27.1</b>
<b>Other Op. income</b>	<b>618</b>	<b>793</b>	<b>(22.1)</b>	<b>354</b>	<b>74.8</b>	<b>972</b>	<b>1,524</b>	<b>(36.3)</b>
<b>Net Sales</b>	<b>55,198</b>	<b>50,383</b>	<b>9.6</b>	<b>55,044</b>	<b>0.3</b>	<b>1,10,242</b>	<b>93,844</b>	<b>17.5</b>
USDINR	74	74	0.8	74	0.5	74	74	(0.5)
US revenue (US\$ mn)	142	141	1.1	141	1.1	283	277	2.3

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 for 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 margins. The company continues to strengthen its revenue streams with a differentiated portfolio, product development capabilities and derisking of the supply chain across its markets.

As per management, Cipla's near-term priorities include continued execution on demand levers, improvement in manpower productivity, active advancement on innovative consumer-centric products to accelerate its global consumer wellness franchise, sustained leadership and growth in respiratory categories such as Albuterol, monitoring of key filings & acceleration of its global lung leadership aspirations, and maximising the value opportunity in US complex generics with steady launches.

We retain BUY and keep our Sep'22 TP at Rs 1,160, based on an unchanged 17x one-year forward EV/EBITDA multiple and implied P/E of 28x. Our target multiple is at the midpoint of the stock's 10-year historical band (12-22x) and 8% lower than our multiple for Sun Pharma (SUNP).

**Fig 3 – Key assumptions**

(Rs mn)	FY21	FY22E	FY23E	FY24E
Revenue	1,91,595	2,16,263	2,35,667	2,59,233
EBITDA	42,524	47,567	50,362	56,938
PAT	24,048	27,604	29,733	35,958
EBITDA Margin (%)	22.2	22.0	21.4	22.0

Source: Company, BOBCAPS Research

**Fig 4 – Peer comparison**

Company	Price (26-Oct-21)	Mcap (US\$ mn)	Rating	EBITDA CAGR (%) (FY21E-FY23E)	P/E (x)		EV/EBITDA (x)		ROE (%)	ROIC (%)
					FY22E	FY23E	FY22E	FY23E	FY22E	FY22E
Aurobindo Pharma	704	5,569	BUY	4.8	12.3	11.2	7.2	6.6	14.2	20.2
Cipla	908	9,859	BUY	8.8	26.5	24.6	14.7	13.9	14.2	21.7
Dr Reddy's Labs	4,666	10,437	BUY	15.2	27.6	21.4	15.4	12.5	15.9	21.6
Lupin	930	5,672	HOLD	19.1	28.6	23.5	12.8	11.0	10.5	17.8
Sun Pharma	814	26,705	BUY	14.3	25.8	22.8	17.6	15.8	15.3	25.4
Divi's Labs	5,019	18,464	HOLD	17.3	52.2	42.9	36.2	30.3	25.7	43.3
Laurus Labs	565	4,106	BUY	16.7	25.5	21.9	17.3	14.7	37.8	36.4
Alkem Labs	3,696	5,949	HOLD	3.3	27.5	23.1	20.0	17.1	23.3	36.1
Alembic Pharma	757	2,001	BUY	(1.1)	20.9	17.7	10.9	9.4	13.3	17.3
Ajanta Pharma	2,118	2,430	BUY	8.8	25.2	20.9	17.6	15.0	22.0	31.3
Eris Life	810	1,470	BUY	19.9	26.5	21.5	20.0	16.4	26.1	27.3
<b>Aggregate</b>				-	<b>27.2</b>	<b>22.9</b>	<b>17.2</b>	<b>14.8</b>	<b>19.8</b>	<b>27.1</b>

Source: BOBCAPS Research

### Key risks

- **Poor US execution:** We expect the US market to contribute meaningfully to profitability in the coming years. Any delay in ramp-up of key launches such as Advair Diskus can potentially erode 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.
- **Regulatory issues:** Failure to get clearance on plants under USFDA observations would affect growth.
- **Drug prices:** Weak drug price hikes in South Africa are another key downside risk.

### Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Ajanta Pharma	AJP IN	2.5	2,118	2,800	BUY
Alembic Pharma	ALPM IN	2.0	757	980	BUY
Alkem Labs	ALKEM IN	5.9	3,696	4,250	HOLD
Aurobindo Pharma	ARBP IN	5.5	704	886	BUY
Cipla	CIPLA IN	9.8	908	1,160	BUY
Divi's Labs	DIVI IN	17.8	5,019	5,540	HOLD
Dr Reddy's Labs	DRRD IN	10.3	4,666	5,500	BUY
Eris Lifesciences	ERIS IN	1.5	810	975	BUY
Laurus Labs	LAURUS IN	4.0	565	715	BUY
Lupin	LPC IN	5.6	930	1,045	HOLD
Sun Pharma	SUNP IN	26.1	814	955	BUY

Source: BOBCAPS Research, NSE | Price as of 26 Oct 2021

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Total revenue</b>	<b>1,71,320</b>	<b>1,91,595</b>	<b>2,16,263</b>	<b>2,35,667</b>	<b>2,59,233</b>
EBITDA	32,060	42,524	47,567	50,362	56,938
Depreciation	11,760	10,677	13,195	13,867	14,539
EBIT	20,300	31,847	34,371	36,494	42,399
Net interest inc./(exp.)	(1,972)	(1,607)	(625)	(390)	(244)
Other inc./(exp.)	3,442	2,660	3,810	4,349	6,768
Exceptional items	0	0	0	0	0
EBT	21,770	32,900	37,557	40,453	48,922
Income taxes	6,312	8,888	9,952	10,720	12,964
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	5	(36)	0	0	0
<b>Reported net profit</b>	<b>15,453</b>	<b>24,048</b>	<b>27,604</b>	<b>29,733</b>	<b>35,958</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>15,453</b>	<b>24,048</b>	<b>27,604</b>	<b>29,733</b>	<b>35,958</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	22,818	20,668	29,447	32,100	35,324
Other current liabilities	10,604	14,709	12,898	14,060	15,472
Provisions	10,815	11,945	13,523	14,741	16,221
Debt funds	28,160	15,375	9,609	6,006	3,754
Other liabilities	0	0	0	0	0
Equity capital	1,613	1,613	1,613	1,613	1,613
Reserves & surplus	1,60,215	1,84,062	2,07,634	2,33,335	2,65,261
Shareholders' fund	1,61,827	1,85,675	2,09,247	2,34,948	2,66,874
<b>Total liab. and equities</b>	<b>2,34,224</b>	<b>2,48,372</b>	<b>2,74,724</b>	<b>3,01,855</b>	<b>3,37,644</b>
Cash and cash eq.	10,039	14,012	20,010	46,878	81,170
Accounts receivables	38,910	34,457	44,171	48,151	52,986
Inventories	43,776	46,692	58,895	64,201	70,648
Other current assets	21,715	21,267	30,095	32,807	36,101
Investments	15,953	28,318	28,318	28,318	28,318
Net fixed assets	51,281	49,563	44,367	38,500	31,960
CWIP	8,245	9,689	9,689	9,689	9,689
Intangible assets	44,305	44,375	39,180	33,312	26,773
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>2,34,224</b>	<b>2,48,372</b>	<b>2,74,724</b>	<b>3,01,855</b>	<b>3,37,644</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Cash flow from operations</b>	<b>33,854</b>	<b>41,404</b>	<b>19,224</b>	<b>37,027</b>	<b>42,280</b>
Capital expenditures	(9,259)	(7,180)	(8,000)	(8,000)	(8,000)
Change in investments	9,586	(12,365)	0	0	0
Other investing cash flows	0	0	0	0	0
<b>Cash flow from investing</b>	<b>327</b>	<b>(19,545)</b>	<b>(8,000)</b>	<b>(8,000)</b>	<b>(8,000)</b>
Equities issued/Others	1	0	0	0	0
Debt raised/repaid	(15,001)	(12,785)	(5,766)	(3,603)	(2,252)
Interest expenses	(1,972)	(1,607)	(625)	(390)	(244)
Dividends paid	(2,419)	(4,032)	(4,032)	(4,032)	(4,032)
Other financing cash flows	(10,941)	539	5,195	5,867	6,539
<b>Cash flow from financing</b>	<b>(30,332)</b>	<b>(17,885)</b>	<b>(5,227)</b>	<b>(2,159)</b>	<b>11</b>
<b>Chg in cash &amp; cash eq.</b>	<b>3,850</b>	<b>3,974</b>	<b>5,997</b>	<b>26,869</b>	<b>34,291</b>
<b>Closing cash &amp; cash eq.</b>	<b>10,038</b>	<b>14,013</b>	<b>20,010</b>	<b>46,878</b>	<b>81,170</b>

### Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	19.2	29.8	34.3	36.9	44.6
Adjusted EPS	19.2	29.8	34.3	36.9	44.6
Dividend per share	3.0	5.0	5.0	5.0	5.0
Book value per share	197.1	227.1	256.3	288.2	327.8

### Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	4.4	3.9	3.3	3.0	2.6
EV/EBITDA	23.4	17.5	15.2	14.0	12.0
Adjusted P/E	47.3	30.4	26.5	24.6	20.3
P/BV	4.6	4.0	3.5	3.1	2.8

### DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	71.0	73.1	73.5	73.5	73.5
Interest burden (PBT/EBIT)	107.2	103.3	109.3	110.8	115.4
EBIT margin (EBIT/Revenue)	11.8	16.6	15.9	15.5	16.4
Asset turnover (Rev./Avg TA)	22.0	24.5	25.8	25.6	25.3
Leverage (Avg TA/Avg Equity)	1.2	1.1	1.1	1.0	1.0
<b>Adjusted ROAE</b>	<b>9.9</b>	<b>14.1</b>	<b>14.2</b>	<b>13.5</b>	<b>14.5</b>

### Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
<b>YoY growth (%)</b>					
Revenue	9.2	11.8	12.9	9.0	10.0
EBITDA	32.3	32.6	11.9	5.9	13.1
Adjusted EPS	131.4	55.6	14.8	7.7	20.9
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	18.7	22.2	22.0	21.4	22.0
EBIT margin	11.8	16.6	15.9	15.5	16.4
Adjusted profit margin	9.0	12.6	12.8	12.6	13.9
Adjusted ROAE	9.9	14.1	14.2	13.5	14.5
ROCE	12.2	17.6	18.2	17.8	19.2
<b>Working capital days (days)</b>					
Receivables	85	66	75	75	75
Inventory	96	90	100	100	100
Payables	50	40	50	50	50
<b>Ratios (x)</b>					
Gross asset turnover	1.2	1.3	1.3	1.4	1.5
Current ratio	2.6	2.5	2.7	3.2	3.6
Net interest coverage ratio	10.3	19.8	55.0	93.5	173.8
<b>Adjusted debt/equity</b>	<b>0.1</b>	<b>(0.1)</b>	<b>(0.2)</b>	<b>(0.3)</b>	<b>(0.4)</b>

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

## Disclaimer

### Recommendation scale: Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

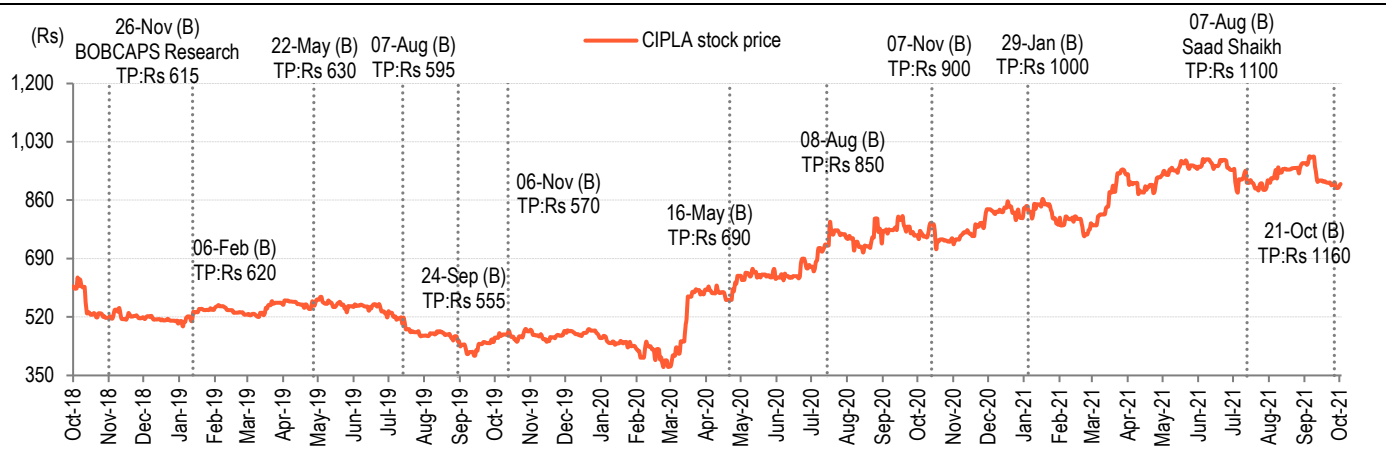
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

### Ratings and Target Price (3-year history): CIPLA (CIPLA IN)



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

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