

BUY

TP: Rs 1,250 | ▲ 21%

CIPLA

| Pharmaceuticals

| 26 January 2023

US-led growth; margins strong

- Q3 revenue grew 6% YoY to Rs 58bn (11% ex-Covid sales last year) driven by US business and despite a sharp decline in SAGA
- Product mix improvement and contribution of gRevlimid aided gross/EBITDA expansion of 460bps/170bps YoY
- We cut FY23-FY24 EBITDA 2-3% and rollover to a revised TP of Rs 1,250 (vs. Rs 1,320); retain BUY

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US-led growth: Cipla reported Q3FY23 revenue growth of 6% YoY to Rs 58.1bn (+11% adjusted for Covid sales in the base quarter), led primarily by 30% YoY growth in the US business to US\$ 195mn (+9% QoQ). US growth was supported by a steady contribution from Lenalidomide and market share expansion in respiratory and peptide products, which offset price erosion in the base business. Domestic market growth was limited to 2% YoY but rises to 11% if we exclude ~Rs 2bn in Covid sales during Q3FY22.

Supply challenges impact SAGA business: SAGA (South Africa, Sub-Saharan Africa and Cipla Global Access) business continued to decline for the third straight quarter, falling 24% YoY marred by supply challenges. Per management, the SAGA business is being transitioned towards the private market as against the earlier low-margin tender business. Management expects sales to normalise from Q1FY24.

International market hit by currency headwinds: International market, impacted by volatile currency, reported YoY growth of 3.3% (6% ex-Covid base quarter sales). The active pharma ingredient (API) business declined 2% YoY. As per management, API inventory levels have normalised for European customers.

Product mix change and new launches lift margins: Despite a sharp decline in SAGA (tender) business, Cipla's gross margin expanded 460bps YoY to 65.5% in Q3, backed by contribution from new launches (including gRevlimid) and an overall mix change. EBITDA margin expansion (+175bps YoY to 24.2%) was despite higher R&D spend for the quarter. The company expects Q4 margins to moderate with seasonality but is confident of achieving its FY23 guidance of 21-22%.

Retain BUY; TP raised to Rs 1,250: Based on a continued slowdown in SAGA business and volatile international/API business, we cut our FY23-FY24 EBITDA estimates by 2-3%. Estimate revision coupled with rollover to 1Y forward earnings leads to a reduced TP of Rs 1,250 (vs. Rs 1,320), based on an unchanged 17x EV/EBITDA multiple – ~10% premium to the stock's 5Y average.

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	CIPLA IN/Rs 1,035
Market cap	US\$ 10.2bn
Free float	63%
3M ADV	US\$ 19.5mn
52wk high/low	Rs 1,185/Rs 881
Promoter/FPI/DII	36%/25%/21%

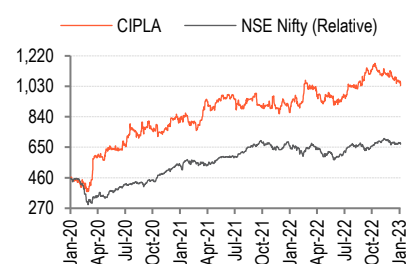
Source: NSE | Price as of 25 Jan 2023

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	2,17,731	2,39,636	2,60,508
EBITDA (Rs mn)	45,625	51,554	60,298
Adj. net profit (Rs mn)	27,086	31,852	39,445
Adj. EPS (Rs)	33.6	39.5	49.0
Consensus EPS (Rs)	33.6	39.1	50.1
Adj. ROAE (%)	13.9	14.5	15.7
Adj. P/E (x)	30.8	26.2	21.1
EV/EBITDA (x)	18.2	15.7	13.2
Adj. EPS growth (%)	12.6	17.6	23.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	9MFY23	9MFY22	YoY (%)
Net Sales	58,101	54,789	6.0	58,285	(0.3)	1,70,138	1,65,030	3.1
EBITDA	14,075	12,310	14.3	13,023	8.1	38,532	38,031	1.3
Depreciation	2,721	2,475	-	2,994	-	8,259	7,616	-
EBIT	11,354	9,835	15.4	10,030	13.2	30,273	30,414	(0.5)
Interest	318	207	-	256	24.5	752	883	-
Other Income	1,144	913	-	1,230	(6.9)	3,408	2,169	-
PBT	12,181	10,541	15.6	11,004	10.7	32,930	31,701	3.9
Less: Taxation	4,100	2,952	-	3,026	-	9,806	8,627	-
Less: Minority Interest	71	304	-	89	-	361	281	-
Recurring PAT	8,010	7,286	9.9	7,889	1.5	22,763	22,793	(0.1)
Exceptional items	0	0	-	0	-	0	(1,246)	-
Reported PAT	8,010	7,286	9.9	7,889	1.5	22,763	21,547	5.6
Key Ratios (%)			(bps)		(bps)			(bps)
Gross Margin	65.5	60.9	462	62.9	257	63.6	61.5	210
EBITDA Margin	24.2	22.5	176	22.3	188	22.6	23.0	(40)
Tax / PBT	33.7	28.0	-	27.5	-	29.8	27.2	-
NPM	13.8	13.3	49	13.5	25	13.4	13.8	-
EPS (Rs)	9.9	9.0	-	9.8	-	28.2	28.3	-

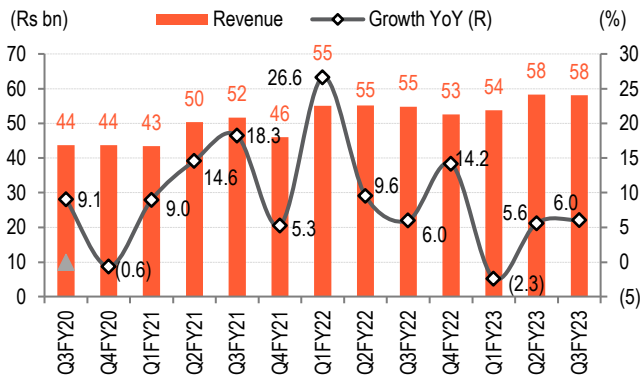
Source: Company, BOBCAPS Research

Fig 2 – Segmental performance

(Rs mn)	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	9MFY23	9MFY22	YoY (%)
Formulations	56,050	52,720	6.3	56,250	(0.4)	1,64,200	1,57,250	4.4
India	25,630	25,180	1.8	25,630	0.0	76,090	76,440	(0.5)
North America	16,000	11,240	42.3	14,320	11.7	42,310	32,170	31.5
SAGA	6,800	8,920	(23.8)	8,670	(21.6)	23,350	27,230	(14.2)
South Africa	5,500	6,230	(11.7)	5,980	(8.0)	17,160	19,670	(12.8)
Others/Global Access	1,300	2,690	(51.7)	2,690	(51.7)	6,190	7,560	(18.1)
International	7,620	7,380	3.3	7,630	(0.1)	22,450	21,410	4.9
APIs	1,470	1,500	(2.0)	1,530	(3.9)	4,350	6,240	(30.3)
Other Op. income	581	569	2.1	505	14.9	1,588	1,541	3.1
Net Sales	58,101	54,789	6.0	58,285	(0.3)	1,70,138	1,65,031	3.1
USDINR	82.1	75.0	9.5	79.9	2.7	80	74	7.5
US revenue (US\$ mn)	195	150	30.0	179	8.8	530	433	22.4

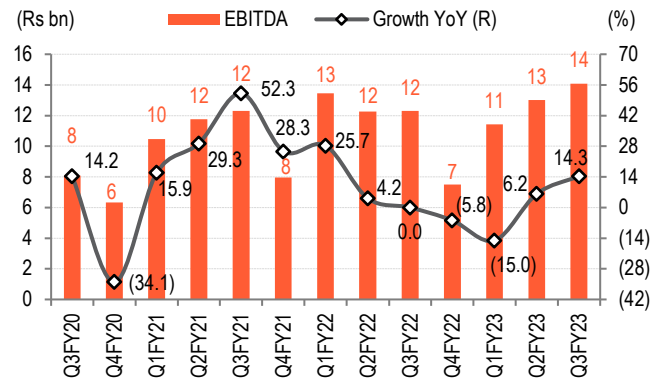
Source: Company, BOBCAPS Research

Fig 3 – Revenue



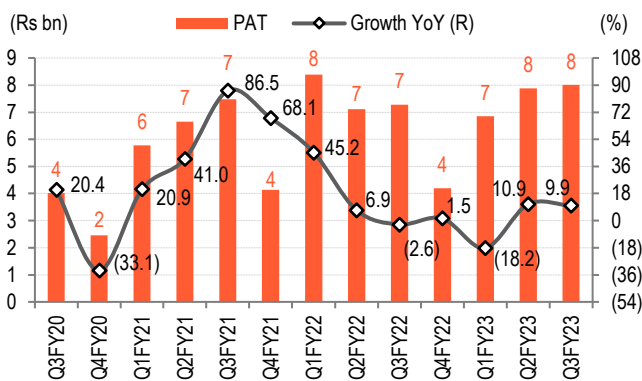
Source: Company, BOBCAPS Research

Fig 4 – EBITDA



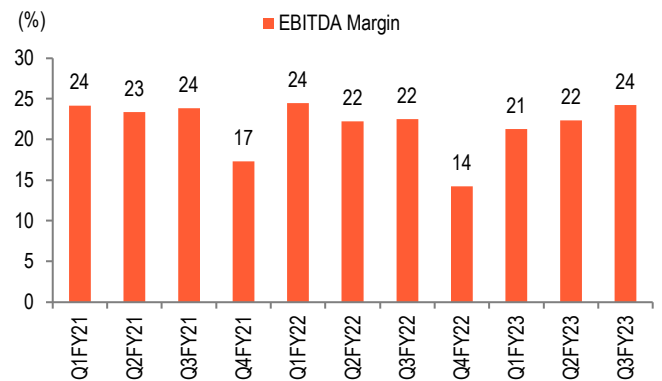
Source: Company, BOBCAPS Research

Fig 5 – PAT



Source: Company, BOBCAPS Research

Fig 6 – EBITDA Margin



Source: Company, BOBCAPS Research

Earnings call highlights

- **Revenue growth:** Cipla reported 6% YoY revenue growth to Rs 58bn in Q3FY23 (11% adjusted for Covid sales of ~Rs 2bn in Q3FY22).
 - **One-India:** The One-India business posted robust double-digit growth across therapies and business segments, at 11% YoY ex-Covid. The chronic/acute share of prescription business was 60:40. Chronic therapies grew in double-digits while acute sales increased 6% YoY.
 - **North America:** The business saw strong traction in respiratory products, further propelled by new launches including peptides.
 - **SAGA:** Supply challenges had an impact on SAGA growth this quarter.
 - **International markets:** Revenue was impacted by currency volatility.
- **Key products:** Cipla's key products did well in Q3 –
 - **gRevlimid:** Contribution from gRevlimid increased YoY but was lower than Q2. The company does not envisage intense competition at least for the next few quarters.

- **Albuterol & Arformoterol:** Market share stands at 17.6% and 38.5% respectively.
- **Lanreotide:** Market share increased from 9.6% in Q2FY23 to 14.1% in Nov'22.
- **Margins:** Reported gross margin stood at 65.5% for the quarter (+460bps YoY) with EBITDA margin expansion at 175bps to 24.2%. The company expects Q4 margins to moderate due to seasonality but indicated that it is on track to achieve FY23 guidance of 21-22%.
- **R&D:** R&D spend increased in Q3 on account of ongoing clinical trials of a respiratory asset as well as other developmental efforts, including contribution to the Kemwell biosimilar JV. R&D guidance for FY23 remains at 6-7% of revenue.
- **Biosimilars:** Cipla's biosimilar JV partner Kemwell is working on two assets, one of which is going into development stage. The company is looking at non-regulated market launch in the next 3-4 years and regulated market rollout in 5-6 years.
- **Inorganic opportunities:** Given the strong cash on the balance sheet, the company is open to inorganic opportunities and evaluating these in domestic and international markets, with a focus on the domestic front.
- **Advair:** Cipla indicated that it had received and replied to minor queries on Advair from the USFDA, with a new target action date (TAD) in the first week of Apr'23.

Valuation methodology

With a strong India franchise, differentiated US pipeline (gAdvair, gAbraxane, peptide injections) and relatively low risk of price erosion in the US market, we believe Cipla is poised to leverage its network reach to launch key generics. We remain positive on the company but trim our FY23/FY24 EBITDA estimates by 3%/2% to factor in the slowdown in SAGA business. Estimate revision coupled with rollover to 1-year forward earnings lead to a reduced TP of Rs 1,250 (vs. Rs 1,320). We continue to value the stock at a 17x EV/EBITDA multiple – ~10% premium to the five-year average, and maintain our BUY rating.

Fig 7 – Revised estimates

(Rs bn)	New			Old			Change (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	239.6	260.5	287.8	245.6	267.3	NA	(2.4)	(2.5)	-
EBITDA	51.6	60.3	69.4	52.9	61.4	NA	(2.5)	(1.8)	-
EBITDA Margin (%)	21.5	23.1	24.1	21.5	23.0	NA	(1bps)	18bps	-
EPS (Rs.)	39.5	49.0	59.2	41.0	49.7	NA	(3.5)	(1.5)	-

Source: BOBCAPS Research

Fig 8 – Key assumptions

Revenue (Rs bn)	FY22	FY23E	FY24E	FY25E
Domestic Formulation	98.3	110.1	126.6	145.6
North America	44.3	55.5	55.2	58.5
SAGA	36.8	33.2	35.0	37.1
International	28.7	30.8	32.6	34.6
API	7.6	8.0	8.8	9.7
Other Operating Income	2.0	2.1	2.3	2.4

Source: Company, BOBCAPS Research

Key risks

Key downside risks to our estimates are:

- **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	1.9	1,199	1,470	HOLD
Alembic Pharma	ALPM IN	1.3	546	615	HOLD
Alkem Labs	ALKEM IN	4.4	3,020	2,700	SELL
Aurobindo Pharma	ARBP IN	3.0	418	635	BUY
Cipla	CIPLA IN	10.2	1,035	1,250	BUY
Divi's Labs	DIVI IN	10.8	3,336	3,450	HOLD
Dr Reddy's Labs	DRRD IN	8.5	4,201	4,700	HOLD
Eris Lifesciences	ERIS IN	1.0	624	810	BUY
Glenmark Life Sciences	GLS IN	0.6	390	535	BUY
Laurus Labs	LAURUS IN	2.2	342	540	HOLD
Lupin	LPC IN	4.2	747	700	HOLD
Sun Pharma	SUNP IN	30.6	1,040	1,100	HOLD

Source: BOBCAPS Research, NSE | Price as of 25 Jan 2023

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Total revenue	1,91,596	2,17,731	2,39,636	2,60,508	2,87,769
EBITDA	42,525	45,625	51,554	60,298	69,425
Depreciation	10,677	10,520	11,370	11,728	12,256
EBIT	31,848	35,106	40,184	48,570	57,168
Net interest inc./(exp.)	(1,607)	(1,064)	(934)	(359)	(276)
Other inc./(exp.)	2,660	2,809	4,086	5,094	7,981
Exceptional items	0	0	0	0	0
EBT	32,901	36,851	43,336	53,305	64,873
Income taxes	8,888	9,338	11,484	13,859	17,191
Extraordinary items	0	(1,821)	0	0	0
Min. int./Inc. from assoc.	(36)	427	0	0	0
Reported net profit	24,049	25,265	31,852	39,445	47,682
Adjustments	0	(1,821)	0	0	0
Adjusted net profit	24,049	27,086	31,852	39,445	47,682

Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Accounts payables	20,668	25,081	29,283	31,829	35,186
Other current liabilities	14,709	8,547	14,251	15,490	17,124
Provisions	11,945	13,212	14,548	15,813	17,481
Debt funds	15,375	10,558	8,121	6,247	4,806
Other liabilities	0	0	0	0	0
Equity capital	1,613	1,614	1,614	1,614	1,614
Reserves & surplus	1,84,062	2,07,512	2,35,330	2,70,741	3,14,389
Shareholders' fund	1,85,675	2,09,125	2,36,943	2,72,355	3,16,002
Total liab. and equities	2,48,372	2,66,523	3,03,146	3,41,734	3,90,598
Cash and cash eq.	14,012	19,285	30,483	62,560	1,00,621
Accounts receivables	34,457	34,244	48,804	53,049	58,643
Inventories	46,692	53,502	65,072	70,731	78,190
Other current assets	21,267	29,490	33,252	36,144	39,955
Investments	28,318	26,120	26,120	26,120	26,120
Net fixed assets	49,563	51,644	48,274	44,545	40,289
CWIP	9,689	7,662	7,662	7,662	7,662
Intangible assets	44,375	44,575	43,479	40,923	39,118
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	2,48,372	2,66,523	3,03,146	3,41,734	3,90,598

Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Cash flow from operations	41,404	21,544	25,506	43,789	50,008
Capital expenditures	(7,180)	(12,615)	(8,000)	(8,000)	(8,000)
Change in investments	(12,365)	2,198	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(19,545)	(10,418)	(8,000)	(8,000)	(8,000)
Equities issued/Others	0	1	0	0	0
Debt raised/repaid	(12,785)	(4,817)	(2,436)	(1,874)	(1,442)
Interest expenses	(1,607)	(1,064)	(934)	(359)	(276)
Dividends paid	(4,032)	(4,034)	(4,034)	(4,034)	(4,034)
Other financing cash flows	538	4,060	1,096	2,556	1,805
Cash flow from financing	(17,886)	(5,854)	(6,308)	(3,712)	(3,947)
Chg in cash & cash eq.	3,974	5,273	11,198	32,078	38,061
Closing cash & cash eq.	14,013	19,285	30,483	62,560	1,00,621

Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23E	FY24E	FY25E
Reported EPS	29.8	31.4	39.5	49.0	59.2
Adjusted EPS	29.8	33.6	39.5	49.0	59.2
Dividend per share	5.0	5.0	5.0	5.0	5.0
Book value per share	227.1	256.0	290.5	334.4	388.5

Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23E	FY24E	FY25E
EV/Sales	4.4	3.8	3.4	3.1	2.7
EV/EBITDA	19.9	18.2	15.7	13.2	11.1
Adjusted P/E	34.7	30.8	26.2	21.1	17.5
P/BV	4.6	4.0	3.6	3.1	2.7

DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23E	FY24E	FY25E
Tax burden (Net profit/PBT)	73.1	73.5	73.5	74.0	73.5
Interest burden (PBT/EBIT)	103.3	105.0	107.8	109.7	113.5
EBIT margin (EBIT/Revenue)	16.6	16.1	16.8	18.6	19.9
Asset turnover (Rev./Avg TA)	24.5	25.9	25.8	24.9	24.0
Leverage (Avg TA/Avg Equity)	1.1	1.1	1.1	1.0	1.0
Adjusted ROAE	14.1	13.9	14.5	15.7	16.4

Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23E	FY24E	FY25E
YoY growth (%)					
Revenue	12.3	13.6	10.1	8.7	10.5
EBITDA	35.8	7.3	13.0	17.0	15.1
Adjusted EPS	63.5	12.6	17.6	23.8	20.9
Profitability & Return ratios (%)					
EBITDA margin	22.2	21.0	21.5	23.1	24.1
EBIT margin	16.6	16.1	16.8	18.6	19.9
Adjusted profit margin	12.6	12.4	13.3	15.1	16.6
Adjusted ROAE	14.1	13.9	14.5	15.7	16.4
ROCE	17.6	18.0	19.1	20.5	21.7
Working capital days (days)					
Receivables	66	58	75	75	75
Inventory	90	91	100	100	100
Payables	40	42	45	45	45
Ratios (x)					
Gross asset turnover	1.3	1.3	1.4	1.4	1.5
Current ratio	2.5	2.9	3.1	3.5	4.0
Net interest coverage ratio	19.8	33.0	43.0	135.2	206.9
Adjusted debt/equity	(0.1)	(0.1)	(0.2)	(0.3)	(0.4)

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

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BUY – Expected return >+15%

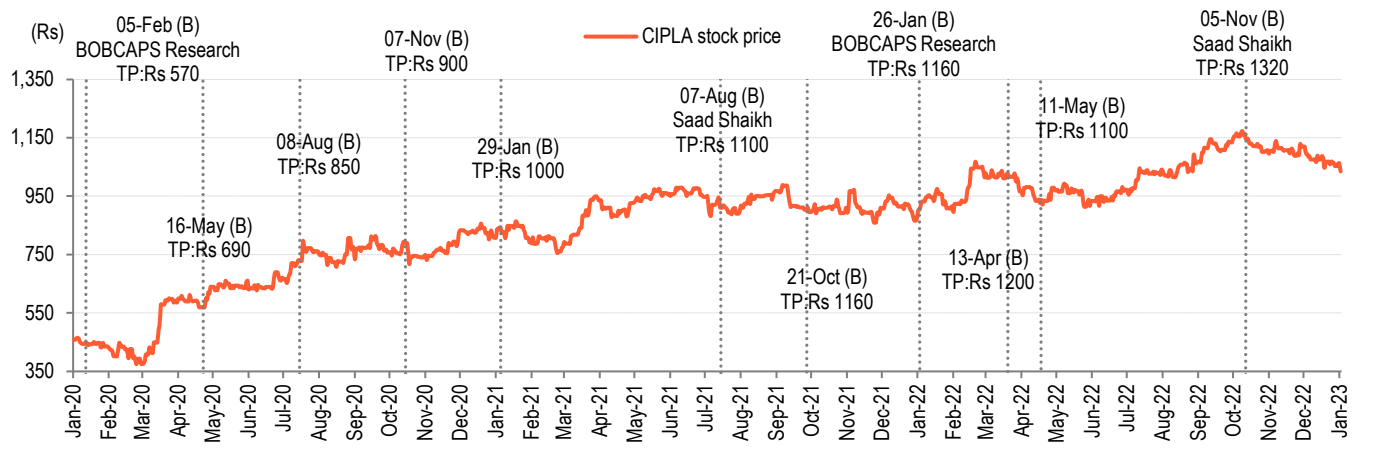
HOLD – Expected return from -6% to +15%

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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