

SELL

TP: Rs 815 | ▼ 7%

LUPIN

| Pharmaceuticals

| 05 February 2022

Major benefits remain back ended, 3Q disappoints

- Q3 revenue growth modest at 4% YoY (+2% QoQ) despite strong US and India formulation business, as API revenue declined 25%
- Higher RM cost and pricing pressure impacted gross margin; adding on a one-off expense, EBITDA margin shrank 1,050bps YoY
- Downgrade from HOLD to SELL as we roll forward to a lower TP of Rs 815 (vs. Rs 1,045) based on 11x FY24E EV/EBITDA (vs. 12x)

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US and India witnessed decline in key portfolio: LPC reported modest 4% YoY revenue growth in Q3FY22 as with 7% YoY growth in the formulations business (US +9% and India +8%) was countered by a 25% YoY drop in API revenue (-4% QoQ). In formulations, the APAC/EMEA geographies posted positive growth of 14%/5% YoY but LATAM/ROW declined by 11%/6%. The US growth was driven gAlbuterol while its core US portfolio witnessed strong price erosion in key products such as Famotidine, gGlumetza and Levothyroxin. India formulations underperformed to the peers due to lower sales of Covid portfolio.

US reports growth with higher Rx share of gAlbuterol: US sales rose 10% QoQ to US\$ 213mn on account 20% Rx share in gAlbuterol, and better traction in new launch of inhalation product. Management however guided to expect the continuation of strong price erosion in US generics as supplies from the peers are gradually normalizing. LPC guided only limited number of products to drive growth in FY23 and FY24 and also depended on faster approval from Goa and Indore plants.

Steep rise in RM cost and one-off expense impact margin: Raw material cost rose 23% YoY to 41% of revenue (vs. 34% of revenue in 3QFY21), depleting gross margin by 650bps YoY to 59.3% (-100bps QoQ). EBITDA margin contracted 1,050bps YoY (-100bps QoQ) to 8.9% due to the lower gross margin and a Rs 1.9bn one-off expense from returns of products in Metformin and bad flu season impacted sales of Oseltamivir. EBITDA margin sans one-off was 13.5% (-585 YoY, -85bps QoQ).

Downgrade to SELL: We cut our FY22-FY24 EBITDA estimates by 23% each with tepid 3QFY22 and soft near-term outlook. On rollover to FY24 valuations, we have a new TP of Rs 815 (vs. Rs 1,045) based on a lower EV/EBITDA multiple of 11x (implied P/E of 21x) from 12x earlier. Our target multiple factors in near-term operational and industry challenges and is at a 30% discount to the aggregate of frontline players such as SUNP, DRRD and CIPLA – downgrade from HOLD to SELL. Lupins EV/EBITDA multiple of 11x is 30% discount to the average multiple of frontline stocks like SUNP, DRRD, CIPLA.

Key changes

Target	Rating
▼	▼

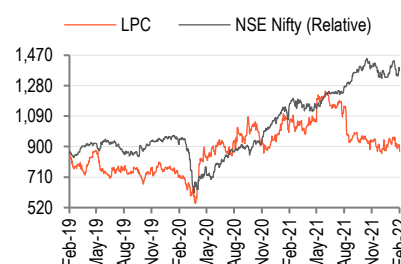
Ticker/Price	LPC IN/Rs 872
Market cap	US\$ 5.3bn
Free float	53%
3M ADV	US\$ 16.3mn
52wk high/low	Rs 1,268/Rs 854
Promoter/FPI/DII	47%/16%/24%

Source: NSE | Price as of 4 Feb 2022

Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	1,51,630	1,60,118	1,72,749
EBITDA (Rs mn)	25,669	24,037	28,133
Adj. net profit (Rs mn)	12,166	11,433	14,062
Adj. EPS (Rs)	26.9	25.3	31.1
Consensus EPS (Rs)	26.9	33.6	43.9
Adj. ROAE (%)	9.2	8.9	11.3
Adj. P/E (x)	32.4	34.5	28.1
EV/EBITDA (x)	16.2	16.1	13.8
Adj. EPS growth (%)	235.1	(6.0)	23.0

Source: Company, Bloomberg, BOBCAPS Research

Stock performance

Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)	9MFY22	9MFY21	YoY (%)
Net Sales	41,609	40,174	3.6	40,913	1.7	1,25,225	1,13,802	10.0
EBITDA	3,698	7,787	(52.5)	5,883	(37.1)	18,857	18,480	2.0
Depreciation	2,034	2,443	-	2,116	-	6,238	6,717	-
EBIT	1,664	5,344	(68.9)	3,767	(55.8)	12,619	11,764	7.3
Interest	334	309	8.0	344	-	1,013	1,088	-
Other Income	341	212	60.9	728	-	1,719	895	-
PBT	1,671	5,247	(68.2)	4,150	(59.7)	13,324	11,570	15.2
Less: Taxation	(3,820)	835	-	(1,099)	-	(2,896)	3,945	-
Less: Minority Interest	35	31	-	32	-	122	68	-
Recurring PAT	5,455	4,381	24.5	5,218	4.5	16,098	7,557	113.0
Exceptional items	0	0	-	(26,198)	-	(26,198)	0	-
Reported PAT	5,455	4,381	24.5	(20,980)	(126.0)	(10,101)	7,557	(233.7)
Key Ratios (%)			(bps)		(bps)			(bps)
Gross Margin	59.3	65.8	(650)	60.2	(97)	61.3	64.5	(318)
EBITDA Margin	8.9	19.4	(1,050)	14.4	(549)	15.1	16.2	(118)
Tax / PBT	(228.7)	15.9	-	(26.5)	-	(21.7)	34.1	-
NPM	13.1	10.9	-	12.8	-	12.9	6.6	-
EPS (Rs)	12.0	9.7	-	11.5	-	35.6	16.7	-

Source: Company, BOBCAPS Research

Fig 2 – Revenue mix

(Rs mn)	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)	9MFY22	9MFY21	YoY (%)
Formulations	38,311	35,735	7.2	37,356	2.6	1,11,848	1,00,410	11.4
US	15,775	14,424	9.4	14,291	10.4	43,396	40,568	7.0
India	14,733	13,669	7.8	15,435	(4.5)	46,530	39,846	16.8
APAC	2,020	1,770	14.1	2,216	(8.9)	6,388	4,917	29.9
EMEA	3,422	3,272	4.6	3,484	(1.8)	9,519	9,031	5.4
LATAM	1,370	1,544	(11.3)	1,274	7.6	3,820	4,014	(4.8)
RoW	991	1,056	(6.2)	656	51.1	2,195	2,034	7.9
APIs	2,564	3,438	(25.4)	2,678	(4.3)	7,701	11,267	(31.6)
Licensing Income	-	-	-	0	-	3,734	-	-
Other Operating income	735	1,001	(26.6)	879	(16.4)	1,942	2,125	(8.6)
Net Sales	41,610	40,174	3.6	40,913	1.7	1,25,225	1,13,802	10.0
USDINR	74	74	0.8	74	0.0	74	74	(0.5)
US revenue (US\$ mn)	213	196	8.5	193	10	587	546	7.5

Source: Company, BOBCAPS Research

Earnings call highlights

- **gAlbuterol led growth in US generics:** With 20% prescription share in gAlbuterol, LPC's US market revenue stood at US\$ 213mn in Q3FY22. Management expects bPegfilgrastim, gSuprep (Tiotropium), gSpiriva and a few more launches to drive US revenues in Q4FY22 and FY23. Lower sales of Famotidine and above-expected product returns of gGlumetza led to a fall in the base portfolio. Levothyroxin witnessed price erosion like other products in the base portfolio, though the molecule is still LPC's biggest product by volume among its key molecules. Solosec in the branded portfolio earned revenue of US\$ 10mn in FY21 with 120 representatives to market the brand in the women's healthcare segment.
- **EBITDA margin guidance:** LPC has guided for a normalised EBITDA margin of 15-16% in the near term. While R&D remains one of the high overheads, management plans to hive off its NCE (new chemical entity) portfolio and is scouting for PE investors. This will help to improve margins as NCE contributes 22% of overall R&D expense.
- **Court cases on gRevlimid settled:** LPC's para-IV challenges on Revlimid have been settled out of court in the US and management expect a risk-free launch only post FY23.
- **Foray into diagnostics:** LPC entered the diagnostics sector in Q3FY22 with 3-4 labs and 200 collection centres. It has another 3-4 managed labs. It is planning a major ramp-up in FY23 and expects growth to rise materially in FY24.
- **USFDA update:** Per management, the Pithampur plant is ready for USFDA CGMP inspection. The Goa plant has received one approval with a further 6-7 approvals likely in FY23 followed by launches. A total of 20 ANDAs are pending from this unit.
- **Capex:** Capex is guided at Rs 5bn-6bn in FY23. LPC plans to close the deal to acquire pharma player Anglo-French by Mar'22. Anglo-French had sales of Rs 950mn in FY21 while the deal is valued at Rs 3.25bn.

Valuation methodology

LPC's gross margin was substantially lower in Q3FY22 (-650bps YoY) due to US price erosion, rising costs and a one-time impact from product returns, which resulted in a 1,050bps YoY contraction in EBITDA margin to 8.9%. Management expects key launches, cost optimisation and operating leverage to kick in ahead.

We cut our FY22-FY24 EBITDA estimates by 23% each with tepid 3QFY22 and soft near-term outlook. On rollover to FY24 valuations, we have a new TP of Rs 815 (vs. Rs 1,045) based on a lower EV/EBITDA multiple of 11x (implied P/E of 21x) from 12x earlier. Our target multiple factors in near-term operational and industry challenges and is at a 30% discount to the aggregate of frontline players such as SUNP, DRRD and CIPLA – downgrade from HOLD to SELL. Lupins EV/EBITDA multiple of 11x is 30% discount to the average multiple of frontline stocks like SUNP, DRRD, CIPLA.

Fig 3 – Revised estimates

(Rs bn)	New			Old			Change (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Sales	160.1	172.7	197.8	164.4	178.7	205.9	(2.6)	(3.3)	(3.9)
EBITDA	24.0	28.1	33.5	31.4	36.4	43.3	(23.6)	(22.8)	(22.7)
EBITDA margin (%)	15.0	16.3	16.9	19.1	20.4	21.0	(411bps)	(410bps)	(410bps)
EPS (Rs)	25.3	31.1	39.0	32.5	39.6	49.0	(22.4)	(21.4)	(20.6)

Source: BOBCAPS Research

Fig 4 – Key assumptions

Revenue (Rs bn)	FY21	FY22E	FY23E	FY24E
India	52.7	62.2	68.2	75.6
US	55.5	54.9	62.9	77.3
EMEA	12.8	13.6	14.6	15.6
ROW	2.5	3.1	3.9	4.8
APAC	5.3	5.5	5.6	5.9
LATAM	5.0	5.3	5.8	6.4
Other EM	1.7	0.0	0.0	0.0
API	13.8	11.7	11.7	12.1
Licensing Income	0.0	3.7	0.0	0.0

Source: Company, BOBCAPS Research

Fig 5 – Peer comparison

Company	Ticker	Rating	Target Price (Rs)	EBITDA CAGR FY21-24E (%)	EPS (Rs)		ROE (%)		Target P/E (x)
					FY22E	FY23E	FY22E	FY23E	
Cipla	CIPLA IN	BUY	1,160	11.0	14.5	12.8	13.6	14.5	16.0
Dr. Reddy's	DRRD IN	HOLD	4,700	10.6	12.1	11.5	17.2	15.5	12.5
Lupin	LPC IN	SELL	815	9.2	14.1	11.8	11.4	13.2	11.0
Sun Pharma	SUNP IN	BUY	1,045	14.9	16.9	15.1	16.1	16.1	18.0

Source: BOBCAPS Research, Bloomberg

Key risks

Key upside risks to our estimates are:

- Faster or in-time approval from key manufacturing plants and approval of CGMP in Indore Pithampur) plant
- Traction in core portfolio with turnaround in competitive scenario
- Ease of margin pressure with traction in India formulations

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Ajanta Pharma	AJP IN	2.5	2,118	2,655	BUY
Alembic Pharma	ALPM IN	2.0	748	980	BUY
Alkem Labs	ALKEM IN	5.6	3,514	4,000	HOLD
Aurobindo Pharma	ARBP IN	5.2	663	886	BUY
Cipla	CIPLA IN	10.2	946	1,160	BUY
Divi's Labs	DIVI IN	15.3	4,305	5,540	HOLD
Dr Reddy's Labs	DRRD IN	9.7	4,352	4,700	HOLD
Eris Lifesciences	ERIS IN	1.3	716	890	BUY
Laurus Labs	LAURUS IN	3.8	529	570	HOLD
Lupin	LPC IN	5.3	872	815	SELL
Sun Pharma	SUNP IN	28.7	894	1,045	BUY

Source: BOBCAPS Research, NSE | Price as of 4 Feb 2022

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Total revenue	1,53,746	1,51,630	1,60,118	1,72,749	1,97,792
EBITDA	23,547	25,669	24,037	28,133	33,470
Depreciation	9,702	8,874	8,269	8,675	9,097
EBIT	13,845	16,795	15,768	19,458	24,373
Net interest inc./(exp.)	(3,630)	(1,406)	(1,337)	(1,296)	(1,285)
Other inc./(exp.)	4,838	1,363	2,078	2,143	2,353
Exceptional items	0	0	0	0	0
EBT	15,053	16,752	16,509	20,305	25,441
Income taxes	11,466	4,485	4,953	6,091	7,632
Extraordinary items	(6,325)	0	(26,198)	0	0
Min. int./Inc. from assoc.	(43)	101	124	151	184
Reported net profit	(2,694)	12,166	(14,766)	14,062	17,625
Adjustments	6,325	0	26,198	0	0
Adjusted net profit	3,631	12,166	11,433	14,062	17,625

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	24,123	20,144	25,831	26,733	30,175
Other current liabilities	45,004	35,585	35,585	35,585	35,585
Provisions	12,040	11,139	7,931	9,228	10,954
Debt funds	42,860	30,656	30,623	30,598	30,577
Other liabilities	0	0	0	0	0
Equity capital	906	907	907	907	907
Reserves & surplus	1,24,906	1,37,674	1,18,601	1,27,422	1,38,479
Shareholders' fund	1,25,812	1,38,581	1,19,508	1,28,330	1,39,386
Total liab. and equities	2,49,839	2,36,104	2,19,479	2,30,473	2,46,677
Cash and cash eq.	24,543	17,425	6,537	11,804	16,412
Accounts receivables	54,459	44,743	48,255	52,061	59,609
Inventories	34,569	40,920	32,901	35,496	40,642
Other current assets	23,746	18,998	19,998	20,998	21,998
Investments	23,743	24,549	24,087	24,087	24,087
Net fixed assets	60,866	59,183	56,914	54,740	52,142
CWIP	9,396	10,663	11,163	11,663	12,163
Intangible assets	18,515	19,624	19,624	19,624	19,624
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	2,49,838	2,36,104	2,19,479	2,30,473	2,46,677

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash flow from operations	50,854	9,989	827	18,830	19,483
Capital expenditures	22,714	(3,497)	(6,500)	(7,000)	(7,000)
Change in investments	(1,041)	(806)	462	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	21,673	(4,302)	(6,038)	(7,000)	(7,000)
Equities issued/Others	1	1	0	0	0
Debt raised/repaid	(39,359)	(12,205)	(32)	(26)	(21)
Interest expenses	(3,630)	(1,406)	(1,337)	(1,296)	(1,285)
Dividends paid	(9,077)	(7,844)	(4,307)	(5,241)	(6,569)
Other financing cash flows	(5,790)	8,647	0	0	0
Cash flow from financing	(57,854)	(12,806)	(5,677)	(6,563)	(7,874)
Chg in cash & cash eq.	14,673	(7,119)	(10,888)	5,267	4,609
Closing cash & cash eq.	24,544	17,425	6,537	11,804	16,412

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	(6.0)	26.9	(32.6)	31.1	39.0
Adjusted EPS	8.0	26.9	25.3	31.1	39.0
Dividend per share	6.0	12.1	9.5	11.6	14.5
Book value per share	277.1	305.0	262.9	282.4	306.8

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	2.9	2.7	2.4	2.3	2.0
EV/EBITDA	18.9	16.2	16.1	13.8	11.7
Adjusted P/E	108.7	32.4	34.5	28.1	22.4
P/BV	3.1	2.9	3.3	3.1	2.8

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	24.1	72.6	69.3	69.3	69.3
Interest burden (PBT/EBIT)	108.7	99.7	104.7	104.4	104.4
EBIT margin (EBIT/Revenue)	9.0	11.1	9.8	11.3	12.3
Asset turnover (Rev./Avg TA)	14.5	15.6	17.6	19.2	20.7
Leverage (Avg TA/Avg Equity)	2.0	1.8	1.8	1.8	1.8
Adjusted ROAE	2.8	9.2	8.9	11.3	13.2

Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	4.8	(1.4)	5.6	7.9	14.5
EBITDA	(8.0)	9.0	(6.4)	17.0	19.0
Adjusted EPS	(56.7)	235.1	(6.0)	23.0	25.3
Profitability & Return ratios (%)					
EBITDA margin	15.3	16.9	15.0	16.3	16.9
EBIT margin	9.0	11.1	9.8	11.3	12.3
Adjusted profit margin	2.4	8.0	7.1	8.1	8.9
Adjusted ROAE	2.8	9.2	8.9	11.3	13.2
ROCE	1.2	7.6	8.1	9.3	10.8
Working capital days (days)					
Receivables	126	110	110	110	110
Inventory	87	87	75	75	75
Payables	162	165	160	160	160
Ratios (x)					
Gross asset turnover	1.2	1.2	1.2	1.3	1.4
Current ratio	1.7	1.8	1.6	1.7	1.8
Net interest coverage ratio	3.8	11.9	11.8	15.0	19.0
Adjusted debt/equity	0.0	(0.1)	0.0	0.0	(0.1)

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

Disclaimer

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

BUY – Expected return >+15%

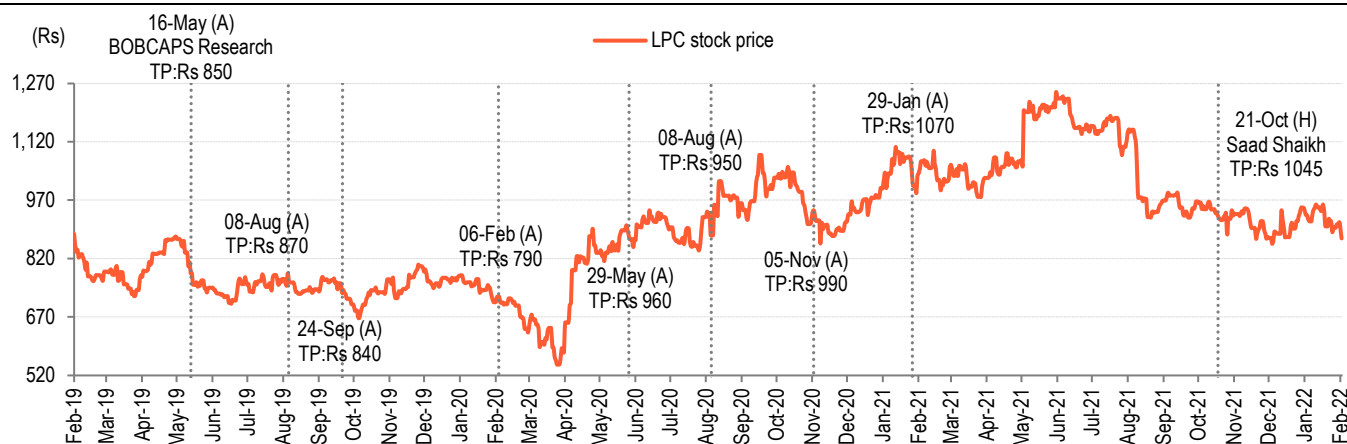
HOLD – Expected return from -6% to +15%

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): LUPIN (LPC IN)



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

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