

Cadila Healthcare

On the road to recovery

We initiate coverage on Cadila with an ADD rating premised on: 1) Recovery in India business post the restructuring measures; we forecast 8% CAGR over FY20-23e; 2) While product concentration risk remains high in the US, timely approval of complex opportunities will be key to offset erosion and drive growth; and 3) R&D investments in vaccines, biosimilars, NCE/NBEs, Covid portfolio adds potential upside opportunities which is currently not factored in our estimates. Moraiya resolution and further debt reduction will be the key catalysts to monitor in the near to medium term. Our target price of Rs445/sh is based on 20x Sep 22 EPS.

India formulations business is restructured, growth trajectory to improve

India business performance is expected to pick up driven by improvement in field force productivity, new launches (including first to market), ramp up in biosimilars (~6% of revenues) and Covid portfolio.

Product concentration risk remains high in US, pipeline execution will be key

US revenues (~USD900mn) have stabilized over the last two years with 2 limited competition assets - Asacol HD and gLialda (Mesalamine franchise) contributing ~30% to revenues. While the near term risk to the franchise is limited (Asacol HD - patent expires in Nov 21, gLialda - competitors are struggling to scale up given product complexity), timely approvals of complex opportunities (transdermals, topicals, injectables) will be key to offset base business erosion.

Investments in vaccines, biosimilars, NCE offers longer term growth visibility

Cadila spends ~35-40% of its R&D on development of vaccines (15+), biosimilars (~21), NCE/NBE (10+) for global markets. In India, ~11 biosimilars and 4 vaccines are currently marketed with revenues of Rs3.4bn and Rs500mn, respectively (as per AIOCD). While the global addressable market opportunity remains large (Exhibit 21, 22), we have not factored any upsides from these programs.

Q2 FY21 highlights

Q2FY21 revenues grew by 13% YoY to Rs38bn driven by robust growth across markets. EBITDA margins were strong at 22.6% (+400bps YoY and 20bps QoQ, cost control) and grew by 38% YoY. Net debt reduced to Rs40bn from Rs67bn in Mar 20 aided by fund raise at Zydus wellness (Rs10bn) and healthy FCF generation (WC day improvement).

Our target price of Rs445/sh provides ~8% upside potential; risks

We initiate coverage on Cadila with an ADD rating and TP of Rs445/sh based on a target PER of 20x Sep 22e EPS, ~15% discount to large cap peers like Cipla, Lupin. Downside risks: higher product concentration risk in the US; delay in Moraiya resolution (WL), higher price erosion, lower growth in India.

Financial Summary

YE Mar (Rs bn)	FY19	FY20	FY21E	FY22E	FY23E
Net Revenues	1,31,656	1,42,531	1,54,581	1,65,299	1,76,883
EBIDTA	29,835	27,834	34,182	36,789	40,253
Rep. PAT	18,488	11,766	18,444	21,542	24,202
EPS (Rs)	17.5	15.0	19.3	21.0	23.6
P/E (x)	23.4	27.3	21.3	19.5	17.4
EV / EBITDA (x)	16.9	18.0	14.2	13.0	11.6
RoCE (%)	11.3	8.6	11.8	12.0	12.2

Source: Company, HSIE Research

ADD

CMP (as on 2 Nov 2020)	Rs 411	
Target Price	Rs 445	
NIFTY	11,669	
KEY CHANGES	OLD	NEW
Rating	-	ADD
Price Target	-	Rs 445
	FY20	FY21E
EPS %	-	-

KEY STOCK DATA

Bloomberg code	CDH IN
No. of Shares (mn)	1,024
MCap (Rs bn) / (\$ mn)	420/5,650
6m avg traded value (Rs mn)	1,929
52 Week high / low	Rs 448/202

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	5.7	26.8	60.7
Relative (%)	0.0	8.9	61.7

SHAREHOLDING PATTERN (%)

	Sep-20	Jun-20
Promoters	74.88	74.88
FIs & Local MFs	12.5	12.6
FPIs	4.38	4.56
Public & Others	8.24	7.96
Pledged Shares	0.00	0.00

Source : BSE

Bansi Desai, CFA

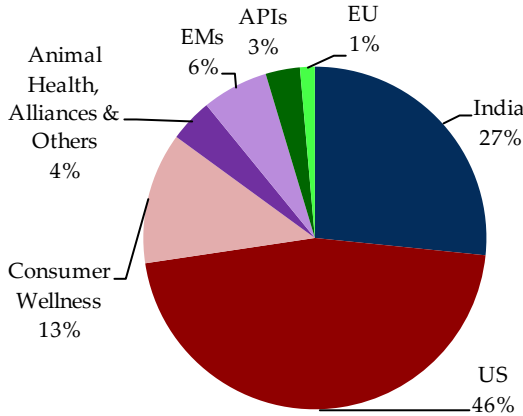
bansi.desai@hdfcsec.com
+91-22-6171-7341

Karan Vora

karan.vora@hdfcsec.com
+91-22-6171-7359

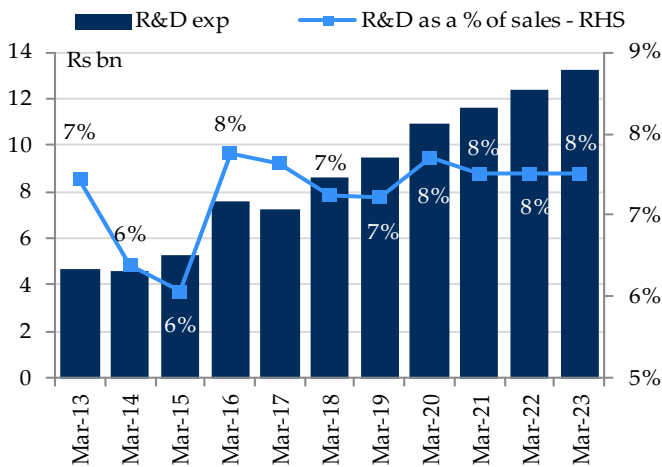
Focus Charts

Exhibit 1: Revenue Split – India and US are dominant markets



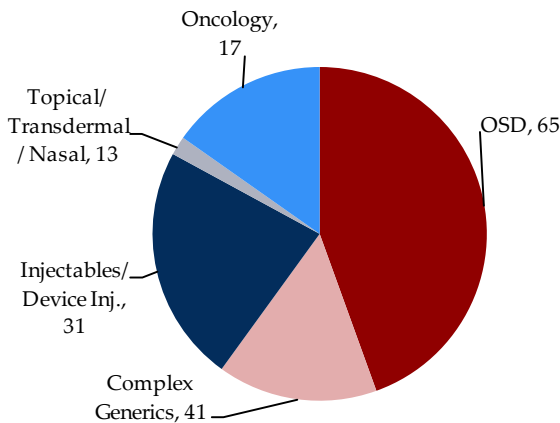
Source: Company, HSIE Research; FY20

Exhibit 3: R&D spends to remain at 7-8% of sales



Source: Company, HSIE Research

Exhibit 5: ~160+ R&D projects under development with addressable market size of ~USD79bn in the US



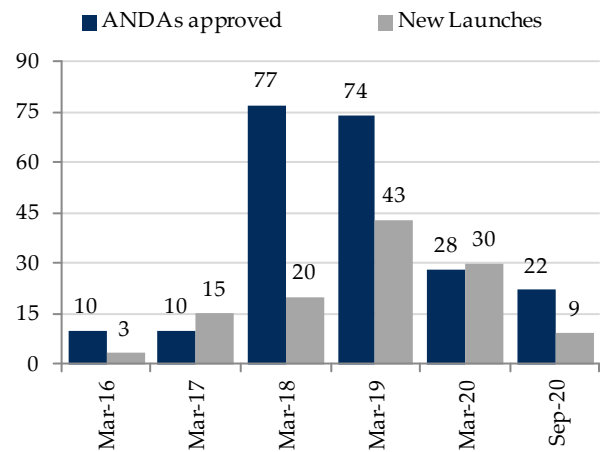
Source: Company, HSIE Research; Size of the pie represents mkt. size

Exhibit 2: India therapeutic performance – Outperformance in AI, Respiratory and Pain

Therapy (Rs mn)	4-yr CAGR		Mkt. share		IPM Rank	
	Cadila	IPM	FY16	FY20	FY16	FY20
Anti-Infective	10.2%	5.7%	3.8%	4.5%	10	8
Cardiac	7.2%	10.1%	5.2%	4.7%	4	7
Respiratory	11.7%	8.6%	5.3%	5.9%	2	3
Gastro	7.0%	7.4%	4.1%	4.0%	5	7
Pain / Analgesics	11.8%	7.8%	5.0%	5.9%	3	3
Gynaec	3.9%	7.0%	7.6%	6.8%	2	3

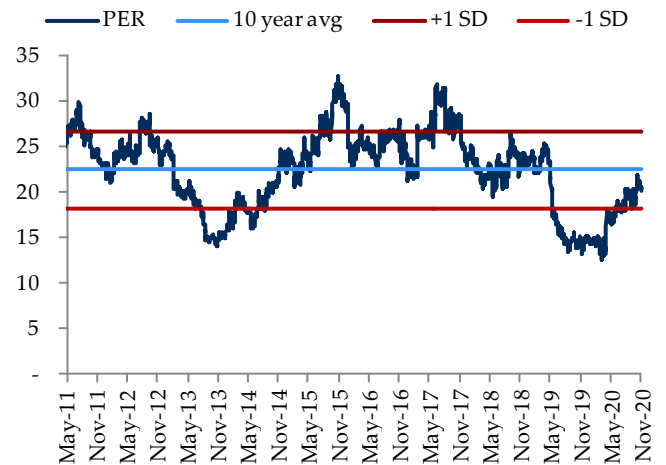
Source: AIOCD AWACS, HSIE Research

Exhibit 4: US – new launches have gathered momentum



Source: Companies, HSIE Research

Exhibit 6: The stock is trading at reasonable valuation of 19.5x FY22e EPS and 17.5x FY23e EPS



Source: Company, HSIE Research, Bloomberg

India business – on recovery path

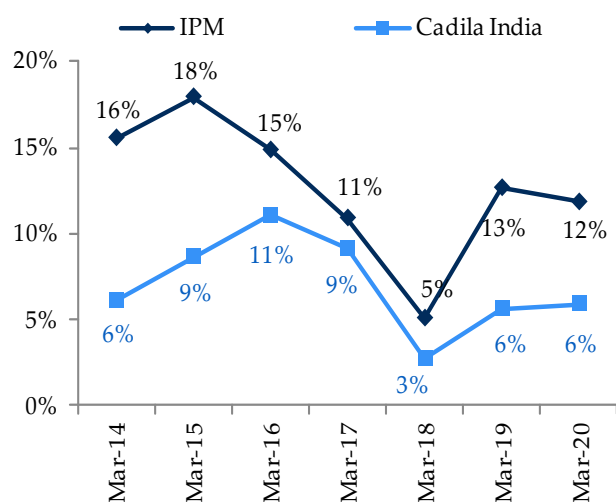
5th largest company in India with ~4.2% share in the IPM

Rank 3 – Respiratory, Pain, Gynaec
Rank 2 – Anti-Neoplastics

(MAT Mar-20, AIOCD)

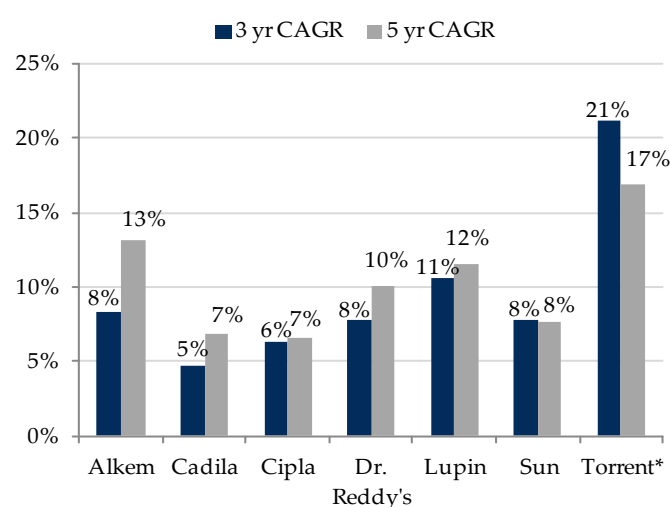
- Cadila’s India formulations performance has been sluggish over the last few years. Several initiatives have been taken to restructure the business in order to enhance marketing & promotion efforts (bifurcated field force into mass and specialty segments), improve margins and supply chain efficiencies which resulted in portfolio rationalization and supply disruptions. Consequently, the business registered muted sales growth of 5.8% CAGR over FY18-20 vs. 9.5% growth of IPM.
- With restructuring in place, we expect sales to report 8% CAGR over FY20-23 driven by improvement in field force productivity (focus on breadth and depth of coverage), new launches (plans to launch 30+ products), ramp up in biosimilars (~11 launches) and Covid portfolio.

Exhibit 7: Cadila has underperformed the IPM growth



Source: AIOCD AWACS, HSIE Research

Exhibit 8: Revenue growth has lagged peers as well

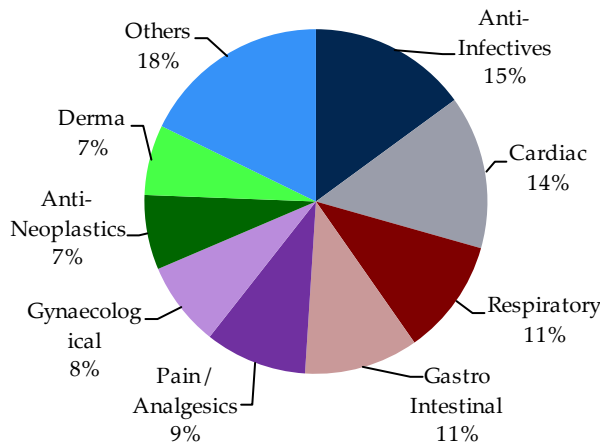


Source: Company, HSIE Research; * includes Unichem acquisition

Therapeutic mix - Acute & sub-chronic segments forms ~69% of revenues

- Cadila arguably has the most diversified portfolio in terms of therapeutic mix (Top 3 therapies account for ~40% of revenues). The company has leadership position (Ranks 3rd) in Respiratory, Pain and Gynaec therapies.
- **Outperformance** - Anti-infective (top 9 out of 10 molecules growing ahead of IPM), Respiratory (presence in fast growing molecules), Pain (novel launch - topical heparin).
- **Underperformance** - Cardiac (high exposure to slower growing molecules such as Atorvastatin, Amlodipine), Gynaec (exposure to slow growing molecules).

Exhibit 9: Diversified portfolio - Acute & sub-chronic segment accounts for ~69% share



Source: AIOCD AWACS, HSIE Research

Exhibit 10: Gaining market share in anti infective, respiratory, pain and losing in cardiac, gynaec

Therapy (Rs mn)	4-yr CAGR		Mkt. share		IPM Rank	
	Cadila	IPM	FY16	FY20	FY16	FY20
Anti-Infective	10.2%	5.7%	3.8%	4.5%	10	8
Cardiac	7.2%	10.1%	5.2%	4.7%	4	7
Respiratory	11.7%	8.6%	5.3%	5.9%	2	3
Gastro	7.0%	7.4%	4.1%	4.0%	5	7
Pain / Analgesics	11.8%	7.8%	5.0%	5.9%	3	3
Gynaec	3.9%	7.0%	7.6%	6.8%	2	3

Source: AIOCD AWACS, HSIE Research

Exhibit 11: However, majority of top 10 molecules are growing higher than category average

Molecule	Brand Name	Therapy	MAT Mar'20	Growth - 4yr CAGR		Mkt. share	
				Zydus*	IPM	FY16	FY20
Theophylline + Etophylline	Deriphyllin, Deriphyllin OD	Respiratory	1,873	11.3%	11.3%	99.9%	100.0%
Hydroquinone + Mometasone + Tretinoin	Skinlite	Derma	1,546	-3.7%	-1.8%	58.9%	54.6%
Atorvastatin	Atorva, Attor	Cardiac	1,420	1.9%	0.0%	15.0%	16.2%
Mifepristone + Misoprostol	Mifegest Kit	Gynaecological	1,393	1.9%	-2.0%	34.6%	40.4%
Pantoprazole	Pantodac	Gastro Intestinal	1,334	7.8%	8.7%	12.8%	12.4%
Nandrolone	Deca Durabolin, Durabolin, Biodebol, Decaneurabol	Hormones	1,222	28.1%	20.2%	63.8%	82.2%
Epoetin Alfa	Zyrop	Blood Related	1,099	15.0%	1.6%	18.2%	29.8%
Unfractionated Heparins - Topical	Thrombophob	Pain/ Analgesics	1,061	16.4%	15.3%	94.4%	98.2%
Amikacin	Amicin	Anti-Infectives	1,010	21.1%	8.8%	12.8%	19.7%
Saroglitazar	Lipaglyn, Bilypsa	Cardiac	966	33.4%	33.4%	100.0%	100.0%
Total			12,925				

Source: AIOCD AWACS, HSIE Research

Biosimilars are an important growth driver

- Cadila is one of the leading players in biosimilars and has a comprehensive portfolio consisting of ~11 brands in India with sales aggregating to Rs3.4bn, registering growth of 23.8% CAGR over the last four years. Biosimilars' sales form ~6% of FY20 revenues (as per AIOCD AWACS).
- It has leadership position (among top 3) in most of the products including key ones such as Adalimumab, Trastuzumab and Bevacizumab.
- In FY20, it received marketing authorization from the DCGI for its first novel biologic 'Rabimabs' in India. The product is launched under the brand name 'TwinRab' in the month of June 2020. It is a cocktail of monoclonal antibodies against rabies virus developed for the post-bite prophylaxis of rabies.

Exhibit 12: Biosimilar portfolio – growing faster with leadership in key products

Biosimilar molecules of the co.	Brand Name	Therapy	MAT Mar'20	Growth - 4yr CAGR		Mkt. Share	
				Zydus*	IPM	FY16	FY20
Epoetin Alfa	Zyrop	Blood Related	1,099	15.0%	1.6%	18.2%	29.8%
Adalimumab	Exemptia	Pain/ Analgesics	512	22.1%	29.2%	99.4%	79.3%
Trastuzumab	Vivitra	Anti-Neoplastics	497	NA	23.4%	0.0%	26.3%
Bevacizumab	Bryxta, Zybev	Anti-Neoplastics	437	NA	37.2%	0.0%	24.2%
Teriparatide	Bonmax PTH	Hormones	325	24.3%	18.5%	17.2%	20.7%
Rituximab	Enfiera, Vortuxi	Anti-Neoplastics	205	NA	8.2%	0.0%	15.3%
Filgrastim	Colstim, Zystim	Anti-Neoplastics	205	-3.5%	-14.2%	18.0%	28.7%
Pegfilgrastim	Pegstim, Pegheal	Anti-Neoplastics	110	-15.8%	-11.9%	35.2%	29.3%
R-FSH	Briogyn, ZY FSH-R	Gynaecological	32	5.7%	3.9%	3.6%	3.8%
Darbepoetin Alfa	Zynesp	Blood Related	31	NA	24.8%	0.0%	2.9%
Retepase	Cathlyse	Cardiac	15	NA	2.0%	0.0%	3.4%
Interferons, Beta	Betaferon*	Anti-Neoplastics	125	69.0%	56.0%	71.9%	99.0%
Total Biosimilars sales			3,592				

Source: AIOCD AWACS, HSIE Research; *with Bayer Zydus

Cadila has 64.8% stake in Zydus Wellness (30th Sept, 20)

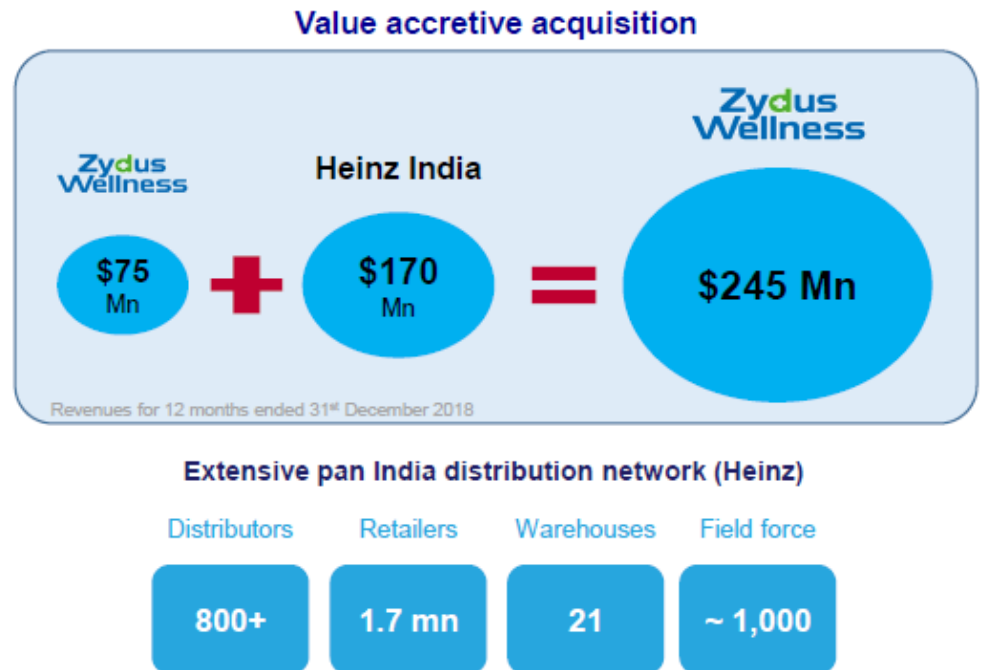
Heinz acquisition completed in Q4FY19 – paid Rs46bn

In Sep'20, Zydus Wellness raised ~Rs10bn via QIP and preferential issue

Zydus Wellness – synergies from acquisition to drive growth and profitability

- Zydus Wellness’ acquisition of Heinz portfolio strengthened the core business with addition of 4 established brands - Complian, Glucon-D, Nycil and Sampriiti Ghee. These brands had sales /EBITDA margin of ~Rs11.5bn/ 20% (MAT Jun’18).
- Combined business to achieve synergies via: a) omni channel strategy; b) increased access to rural markets; c) double the reach; d) enhanced engagement with key accounts; e) benefits from wider talent pool and capabilities; f) revenue and cost synergies.

Exhibit 13: Zydus Wellness – Heinz adds scale and distribution reach



Source: Company, HSIE Research; Revenues for MAT Dec'18

- We forecast ~6% revenue CAGR over the next three years driven by market share gains, line extensions and focused promotion efforts including medical marketing route for relevant brands. With large part of investments done, EBITDA margins should improve from current levels of ~19% (as of FY20).

Exhibit 14: Zydus Wellness – Leadership in niche categories

Brands	Addressable mkt. (Rs bn)	Zydus share (FY20)	Zydus Rank	Mkt. growth (3-yr CAGR)
Sugarfree*	3.9	94.0%	1	NA
Nutralite*	~7.0	NA	1	NA
Everyuth	29.5	6.0%	1^	~10%
Nycil	7.6	34.4%	1	NA
Complan	73.0	5.4%	5	6.0%
Glucon-D	9.8	59.0%	1	11.0%
Sampriiti Ghee	NA	NA	NA	NA

Source: Company, HSIE Research; *Sugarfree & Nutralite mkt. size as of Dec'19, ^Rank 1 in peel-off mask and scrub categories with 77.9% and 32.5% share respectively, FY20

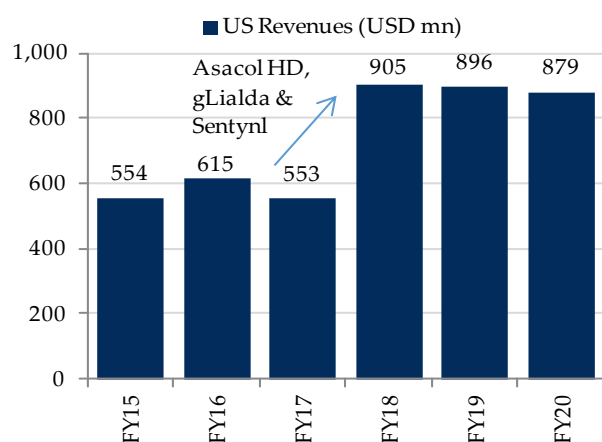
US – Product concentration risk remains high, pipeline offers longer term visibility

Plans to file 30-35 ANDAs in FY21 and 40+ ANDAs in FY22

96 Pending ANDAs

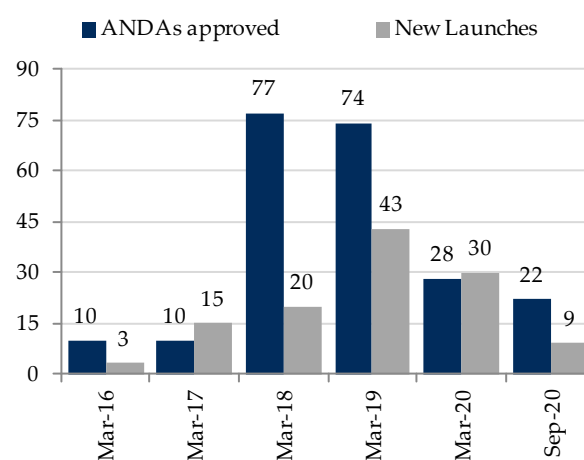
- Cadila’s US business (~USD900mn) has remained stable over the last two years. Two key assets - Asacol HD (only player) and gLialda (Limited competition – Teva, Sun, Mylan) contribute ~30% of US revenues. The patent for Asacol HD expires in Nov 2021 (only one filer known). In gLialda, other generic players have struggled in scaling up the market share given the complexity around the product. Consequently, Cadila has been able to maintain dominant market share in the product. Cadila expects US business to grow in single digit in FY21 driven by ~30+ launches in the year.
- We estimate US sales to post 5.7% CAGR from ~USD906mn in FY20 to USD998mn in FY23e as new launches including complex ones such as transdermals, topicals and injectables offsets price erosion in the base portfolio.

Exhibit 15: USD revenues have largely remained stable



Source: Company, HSIE Research

Exhibit 16: New launches expected to gather pace



Source: Company, HSIE Research

Exhibit 17: Injectables portfolio in the US - Future pipeline has 60%+ complex opportunities

Particulars	Regular	Complex	Total	Mkt size (USD bn)
Approved	51	2	53	2bn
Filed awaiting approval	9	6	15	6bn
Under development	24	15	39	20bn

Source: Company, HSIE Research

Exhibit 18: Complex pipeline under development

Particulars	Oral IR	Generic Complex	Injectables/ Device Inj.	Topical/ Transdermal/ Nasal	Oncology
Product under development	65	41	31	13	17
Addressable mkt size (USD bn)	35.1	12.2	18.1	1.4	12.0
Filing Target	Over 3-4 years	By 2022	Over 3-4 years	Over 3-4 years	Over 3-4 years
Products approved/ under approval	218	95	47	36	42
Addressable mkt size (USD bn)	71.0	24.3	5.3	2.2	16.4
Revenue generation	Ongoing	Ongoing	Ongoing	Ongoing	Ongoing

Source: Company, HSIE Research

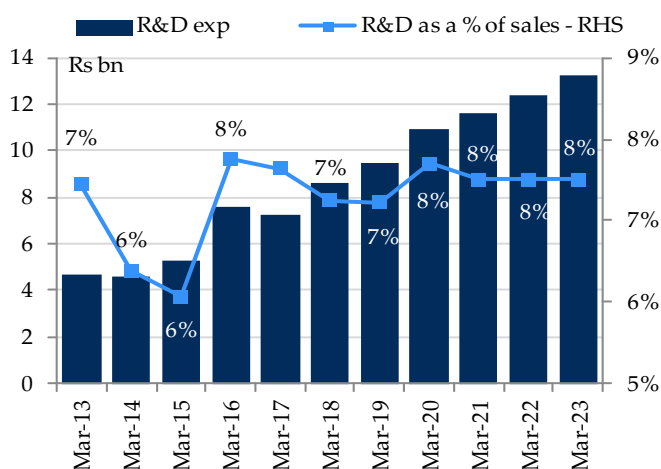
FTFs/ Limited competition opportunities in mid to long term

- Cadila has 28 products which are either potential FTFs or limited competition opportunities with addressable market size of USD37bn. The potential upside is pegged at an annual value of USD560mn by the company (break up - 32%/68% - FTFs/Limited competition and 59%/41% - Filed/In-development status)

R&D spends to remain at 7-8% of sales

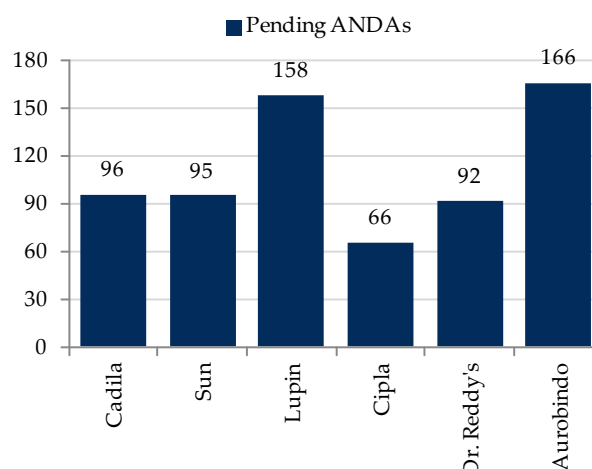
- Cadila spends almost ~35-40% of R&D towards development of vaccines, biologics/biosimilars and NCE/NBE. The balance is largely for the US generics market.

Exhibit 19: R&D is likely to remain at 7-8% of sales



Source: Company, HSIE Research

Exhibit 20: Pending ANDA pipeline



Source: Company, HSIE Research

Vaccines could be an emerging opportunity for India and EM markets

- The revenue contribution from vaccines in India is limited to ~Rs500mn (MAT Mar'20, AIOCD).
- Cadila is also developing a Covid vaccine ZyCOV-D which is currently undergoing Phase-II trials.
- Investment outlay on vaccines has been ~Rs1.5bn so far (ex-Covid). Further investments will depend upon the scale up, the market it intends to target and progress on Covid vaccine plans.

Exhibit 21: Vaccines Portfolio – 15 vaccines under development

Type of Vaccine	Indication	Addressable Global Market	Addressable Market opportunity
Pediatric Vaccine	DTP, Measles, MR, MMR, TCV, Varicella Vaccine	USD14bn (15 vaccines)	India Private (USD70mn) India Public (USD220mn) WHO supplies (USD1.8bn) (4 products marketed)
Adult Vaccine	Flu, HPV Vaccines		
Tropical Diseases	Malaria & Chikungunya vaccines		
Rabies Vaccine	Rabies vaccine, TwinRab		
Hepatitis Vaccine	Hep A, Hep B, Hep E vaccines		

Source: Company, HSIE Research

Biosimilars – A comprehensive pipeline

- Cadila’s pipeline comprise of 6 novel biologics and 21 biosimilars (both in the development stage as well as launched stage) and covers therapeutic areas such as oncology, autoimmune disease, nephrology, ophthalmology, inflammation, rheumatology, hepatology, infectious disease etc.

Exhibit 22: Biosimilar portfolio

Drug	2019 Brand Sales (USD bn)	Competitive Intensity*	Zydus Portfolio
Adalimumab (Inflammation)	19.2	High	✓ Portfolio initiated/completed
Trastuzumab (Onco)	6.1	High	
Pegfilgrastim/ PEG G-CSF (Onco)	3.5	High	
Bevacizumab (Onco)	7.1	High	
Peg-EPO (Onco/ Nephro)	1.1	Medium	
Denosumab (Osteoporosis)	5.1	Low	
TDM-1 (Onco)	1.4	Low	
Onco Segment	3.5	Medium	
Ophthal Segment	8.0	Medium	
Onco Segment	8.1	Low	
Onco Segment	1.5	Low	✓ Portfolio Planned
Respiratory Segment	1.0	NA	
Onco Segment	3.0	Low	- Not planned
GI Segment	6.6	High	
Respiratory Segment	0.7	Low	
Autoimmune Segment	3.4	Low	
	79.2		

Source: Company, HSIE Research; *No. of players - High: >5, Medium: 2-5, Low: <2; Blue - Portfolio Initiated/ completed, Grey - Portfolio planned

Exhibit 23: NCE pipeline under development

Project	Target	Indication	Drug Dis-covery	Lead Opti-mization	Pre-clinical dev.	IND	Phase I	Phase II	Phase III	NDA	Marketed
Desidustat	HIF-PH Inhibitor	Anemia-CKD-NKD/D	[Progress bar]								
		Covid-19	[Progress bar]								
		Chemo ind. anemia	[Progress bar]								
ZRC-3278/ MMV 253	V-Type H+ ATPase	Malaria (MMV)	[Progress bar]								
ZYBK2	HLA-DRB1 shared epitope	RA	[Progress bar]								

Source: Company, HSIE Research

Exhibit 24: NBE pipeline under development

Project	Indication	Cloning	Process development	Pre-clinical	Reg. Permission	Clinical development	Marketing Authorization
NBEs							
TwinRab	Anti Rabies Mab's	[Progress bar]					
ZRC-NB-3224	AMD	[Progress bar]					
ZRC-3297	Autoimmune	[Progress bar]					
ZRC-3298	Oncology	[Progress bar]					
ADC 2	Oncology	[Progress bar]					
ADC 3	Oncology	[Progress bar]					

Source: Company, HSIE Research

Q2FY21 result highlights

Revenues grew by 13.5% led by robust growth across regions

While revenues from key geographies (US, India & EMs) grew in mid-teens, Animal Health & APIs recorded solid double digit growths

EBITDA margins expanded by ~400bps YoY on the back of strong staff & other cost controls despite flattish GMs

Interest expenses almost halved YoY on deleveraging

Adjusted PAT was up 61% YoY on the back of stronger top-line growth, solid (other) cost control and reduced financial leverage

Exhibit 25: Quarterly Financial Snapshot

(INR mn)	2QFY21	2QFY20	YoY (%)	1QFY21	QoQ (%)
Total Revenues	38,200	33,666	13.5	36,399	4.9
Gross Profit	24,977	22,101	13.0	23,896	4.5
EBITDA	8,634	6,256	38.0	8,154	5.9
Depreciation exp.	1,790	1,723	3.9	1,768	1.2
Interest exp.	457	897	(49.1)	677	(32.5)
Operating Inc. / (Loss)	6,387	3,636	75.7	5,709	11.9
Non-operating income	275	269	2.2	225	22.2
PBT	6,662	3,905	70.6	5,934	12.3
Income tax benefit / (exp.)	1,106	395	180.0	1,235	(10.4)
Minority & JVs	(498)	(243)	104.9	159	(413.2)
Recurring PAT	6,054	3,753	61.3	4,540	33.3
Extra-ordinary items	1,320	2,681	(50.8)	-	NA
Reported PAT	4,734	1,072	341.6	4,540	4.3

Source: Company, HSIE Research

Exhibit 26: Margin Analysis

Margin Analysis	2QFY21	2QFY20	YoY (bps)	1QFY21	QoQ (bps)
Material Expenses % Net Sales	34.6	34.4	26	34.3	27
Mfg. & Other Expenses % Net Sales	26.6	29.3	(270)	25.8	83
EBITDA Margin (%)	22.6	18.6	402	22.4	20
Tax Rate (%)	16.6	10.1	649	20.8	(421)
APAT Margin (%)	15.8	11.1	470	12.5	338

Source: Company, HSIE Research

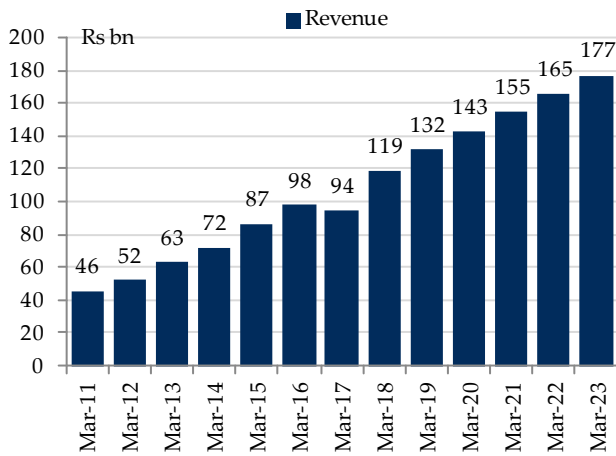
Exhibit 27: Segmental Performance Analysis

Segment Performance (INR mn)	2QFY21	2QFY20	YoY (%)	1QFY21	QoQ (%)
Key Markets	30,321	26,451	14.6	26,899	12.7
US Formulations	17,090	14,484	18.0	16,232	5.3
India	10,870	9,778	11.2	8,292	31.1
Emerging Markets	2,361	2,189	7.9	2,375	(0.6)
Other Businesses and Alliances	7,302	5,991	21.9	8,594	(15.0)
Europe Formulations	546	407	34.2	489	11.7
Consumer Wellness	3,352	3,172	5.7	5,316	(36.9)
Animal Health & Others	1,611	1,348	19.5	1,252	28.7
APIs	1,597	1,049	52.2	1,309	22.0
Alliances	196	15	1,206.7	228	(14.0)
Total	37,623	32,442	16.0	35,493	6.0
Others	577	1,225	(52.9)	906	(36.3)
Total Revenues	38,200	33,667	13.5	36,399	4.9

Source: Company, HSIE Research

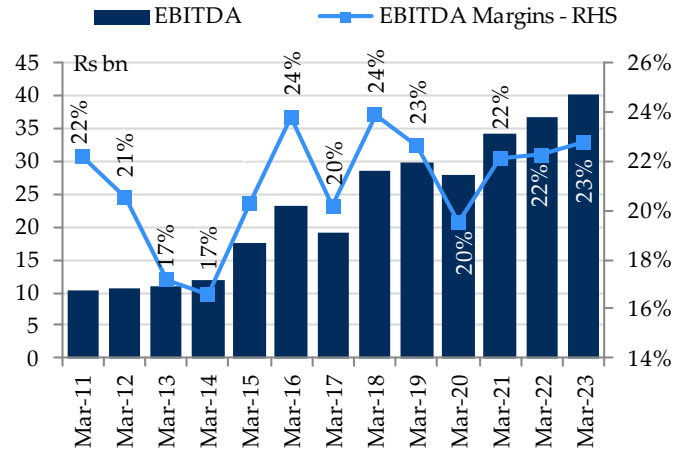
Financial Metrics

Exhibit 28: Revenues are expected to grow by 8% CAGR over FY20-23



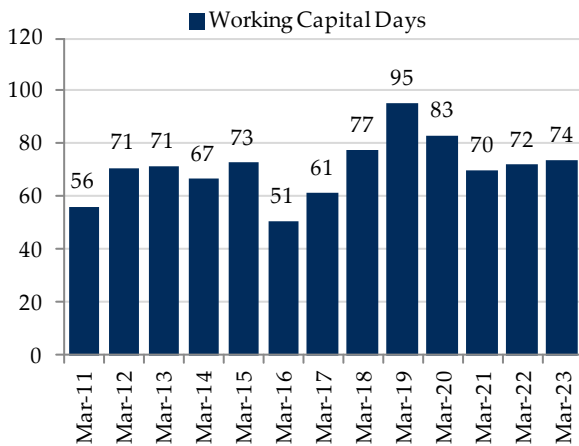
Source: Company, HSIE Research

Exhibit 29: EBITDA margins are likely to improve 320bps over FY20-23e



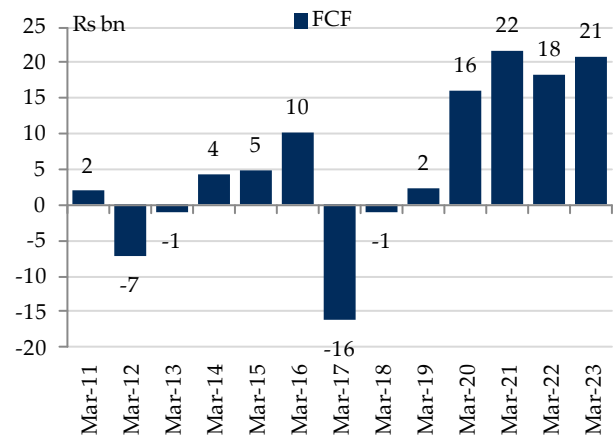
Source: Company, HSIE Research

Exhibit 30: Working capital days have improved in H1FY21 to ~70 days



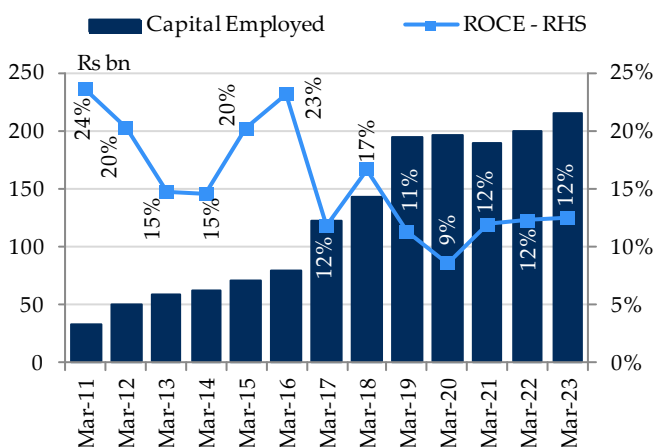
Source: Company, HSIE Research

Exhibit 31: Strong FCF generation to aid further debt reduction



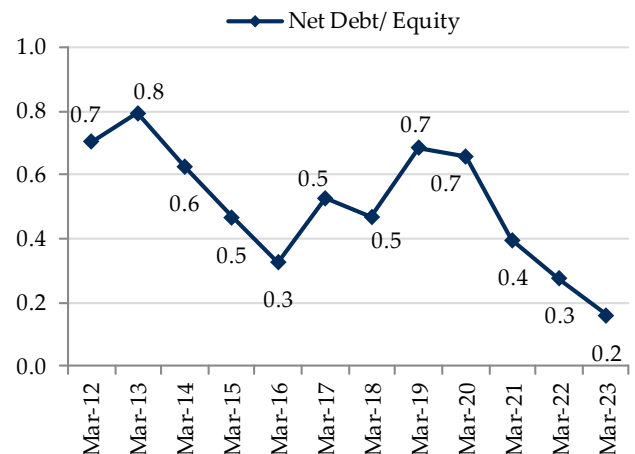
Source: Company, HSIE Research

Exhibit 32: ROCE to improve by 300bps in next 3 years



Source: Company, HSIE Research

Exhibit 33: Leverage to reduce to 0.2x by FY23e



Source: Company, HSIE Research

Valuation and risks

- We assign an ADD rating to Cadila with a target price of Rs445 based on 20x Sep'22 EPS. Cadila's India business performance has lagged peers and IPM over the last few years, however with the restructuring efforts undertaken; we expect the business to grow at 8% CAGR over FY20-23e. US accounts for 45% of revenues and is likely to grow at 6% CAGR over FY20-23e. Product concentration risk remains high in the US with 2 products (Mesalamine franchise) accounting for ~30% of US revenues. Resolution of warning letter at Moraiya and further debt reduction will be the key catalysts to monitor in the near to medium term. Our target multiple of 20x Sep 22 EPS is at 15% discount to large cap peers like Cipla and Lupin.

Exhibit 34: The stock is trading at an attractive valuation of 19.5x FY22e EPS and 17.5x FY23e EPS



Source: Bloomberg, HSIE Research

Risks to our thesis

- India - Expansion of NLEM (national list of essential medicines) coverage, capping of trade margins, slowdown in IPM can adversely impact growth.
- US - High concentration risk, delay in resolving warning letter at Moraiya, higher price erosion, delay in product approvals and launches in US.

Peer set Comparison

Domestic	M.Cap (Rs bn)	CMP (Rs./ Sh)	RECO	TP	EV/ EBITDA (X)			ROE			PER(X)			CAGR (FY20-23E)	
					21E	22E	23E	21E	22E	23E	21E	22E	23E	EPS	Revenue
Aurobindo	446	761	BUY	1,015	8.8	7.9	6.8	18.2	16.5	15.4	14.0	13.2	12.2	10.7%	8.2%
Cadila	420	411	ADD	445	14.2	13.0	11.6	17.9	17.3	17.2	21.3	19.5	17.4	16.3%	7.5%
Cipla	606	751	BUY	855	15.0	12.7	11.0	13.8	14.2	14.3	26.8	23.0	20.1	27.3%	10.3%
Dr. Reddy's	808	4,859	ADD	5,390	15.8	13.4	11.7	17.4	18.2	17.9	26.2	21.5	18.7	16.6%	14.4%
Lupin	414	913	BUY	1,185	19.3	14.2	11.7	10.0	14.2	16.1	38.6	24.7	19.0	38.5%^	11.8%
Sun	1,126	469	ADD	570	15.7	13.2	11.4	3.3	12.4	12.5	26.1	21.1	18.5	18.1%	7.3%
Torrent	431	2,544	ADD	2,675	18.9	17.1	14.7	25.6	26.4	29.2	34.7	30.7	25.2	20.3%	8.7%
Alkem	318	2,659	NR	NA	16.8	15.5	14.1	21.1	19.9	19.3	22.2	20.4	18.2	15.8%	11.4%
Glenmark	134	473	NR	NA	8.8	8.1	7.5	13.3	13.1	13.9	15.2	13.5	11.4	14.8%	8.4%
Ipca Labs	292	2,302	NR	NA	19.6	19.2	16.7	25.6	21.4	20.0	27.0	26.3	23.1	27.6%	14.7%
Eris LS	70	511	NR	NA	17.2	15.5	14.1	23.7	24.0	24.6	21.1	18.7	16.1	13.7%	11.4%

Source: Bloomberg, HSIE Research; ^PBT for Lupin

Financials

Consolidated Income Statement

Year to March (INR mn)	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Revenues	97,832	94,295	1,19,049	1,31,656	1,42,531	1,54,581	1,65,299	1,76,883
Growth (%)	13	-4	26	11	8	8	7	7
Raw material	32,770	34,451	41,220	47,164	49,200	53,320	57,028	61,024
Gross Profit	65,062	59,844	77,829	84,492	93,331	1,01,261	1,08,271	1,15,858
Gross Margins	66.5	63.5	65.4	64.2	65.5	65.5	65.5	65.5
Employee cost	13,663	15,348	18,545	21,241	24,145	26,560	29,215	32,137
Other expenses	28,114	25,460	30,809	33,416	41,352	40,520	42,267	43,468
EBITDA	23,285	19,036	28,475	29,835	27,834	34,182	36,789	40,253
Growth (%)	33	-18	50	5	-7	23	8	9
Margins (%)	23.8	20.2	23.9	22.7	19.5	22.1	22.3	22.8
Depreciation	3,022	3,750	5,388	5,986	6,965	7,364	7,730	8,117
Other income	941	1,286	1,132	1,347	1,139	1,083	1,120	1,305
Interest	486	450	911	1,935	3,418	2,922	2,369	2,220
PBT	20,718	16,122	23,308	23,261	18,590	24,979	27,810	31,221
Tax	5,711	1,289	5,644	5,303	3,198	5,065	6,118	6,869
Effective tax rate (%)	27.6	8.0	24.2	22.8	17.2	20.3	22.0	22.0
Recurring PAT	14,707	14,880	17,946	17,928	15,402	19,764	21,542	24,202
Extraordinary items	569	3	-	768	3,636	-1,320	-	-
MI/share of Profit/loss in JV	-	338	628	469	288	500	500	500
Reported PAT	15,226	14,877	17,946	18,488	11,766	21,084	21,542	24,202

Source: Company, HSIE Research

Consolidated Balance Sheet

Year to March (INR mn)	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Equity capital	1,024	1,024	1,024	1,024	1,024	1,024	1,024	1,024
Reserves and surplus	52,495	68,576	86,421	1,02,839	1,02,733	1,16,656	1,31,037	1,48,078
Shareholder's funds	53,519	69,600	87,445	1,03,863	1,03,757	1,17,680	1,32,061	1,49,102
Minority Interest	1,354	1,561	1,910	12,929	13,347	19,997	20,647	21,297
Total debt	24,420	52,072	54,067	78,994	79,993	57,493	53,993	50,493
Total Liabilities	80,300	1,25,025	1,46,890	1,99,062	1,99,667	1,97,740	2,09,271	2,23,462
Net fixed assets	37,481	57,700	64,826	1,21,637	1,22,305	1,22,941	1,24,211	1,25,094
Capital work-in-progress	9,710	15,433	15,272	8,372	7,415	7,415	7,415	7,415
Investments	3,368	4,348	7,457	5,440	6,209	6,709	7,209	7,709
Inventories	14,512	18,037	23,853	26,880	27,890	28,799	30,796	32,953
Debtors	16,804	22,775	32,063	39,508	36,632	35,998	38,494	41,192
Cash & bank balance	6,953	15,435	13,149	7,788	11,777	11,063	17,551	26,815
Loans and Advances	7,619	14,994	13,549	15,505	14,470	15,064	15,718	16,436
Other current assets	3,716	3,485	10,192	9,701	10,168	10,168	10,168	10,168
Total current assets	38,269	56,247	69,065	74,176	76,299	75,860	86,841	1,00,960
Creditors	13,449	16,736	18,884	19,226	20,310	23,293	24,908	26,654
Provisions	2,146	2,201	3,081	3,735	5,075	5,310	5,569	5,854
Net current assets	22,122	32,550	45,494	48,108	49,268	45,611	54,718	66,807
Total net assets	80,300	1,25,025	1,46,890	1,99,062	1,99,667	1,97,740	2,09,271	2,23,462

Source: Company, HSIE Research

Consolidated Cash Flow

Year to March (INR mn)	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Net Profit Before Tax	21,237	16,119	23,120	23,821	14,954	24,979	27,810	31,221
Depreciation	3,022	3,750	5,405	5,986	6,965	7,364	7,730	8,117
Cash flow before WC	24,532	19,456	29,363	30,464	25,964	34,182	36,789	40,253
WC changes	2,656	-3,728	-13,839	-9,717	1,294	2,349	-3,273	-3,544
Taxes paid	-6,618	-2,376	-6,023	-6,754	-3,025	-5,065	-6,118	-6,869
Cash flow from operations	19,938	13,495	9,193	12,819	25,054	32,785	27,398	29,840
Capex	-9,663	-29,734	-10,353	-10,464	-8,888	-8,000	-9,000	-9,000
Cash flow from investing	-9,039	-29,103	-9,737	-42,387	-10,123	-6,917	-7,880	-7,695
Borrowings (net)	-2,093	27,652	1,574	23,955	-3,489	-22,500	-3,500	-3,500
Interest paid	-465	-556	-1,049	-795	1,116	-2,922	-2,369	-2,220
Dividends paid	-6,969	-3,938	-10	-4,314	-8,569	-7,161	-7,161	-7,161
Cash flow from financing	-9,527	23,158	515	18,846	-10,942	-26,583	-13,030	-12,881
Net change in cash	1,372	7,550	-29	-10,722	3,989	-714	6,488	9,264
Beginning cash	7,904	6,953	15,926	15,897	7,788	11,777	11,063	17,551
Closing cash	9,276	14,503	15,897	7,788	11,777	11,063	17,551	26,815
Free cash flow	10,275	-16,239	-1,160	2,355	16,166	24,785	18,398	20,840

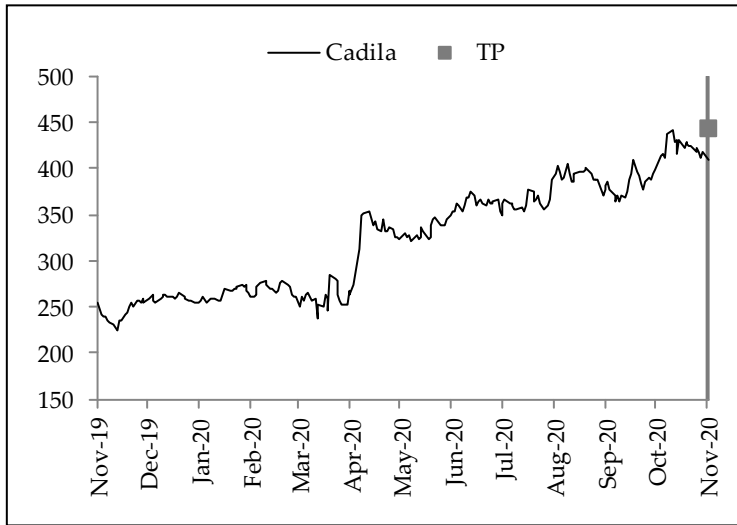
Source: Company, HSIE Research

Key Ratios

Year to March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
PROFITABILITY (%)								
GPM	66.5	63.5	65.4	64.2	65.5	65.5	65.5	65.5
EBITDA Margin	23.8	20.2	23.9	22.7	19.5	22.1	22.3	22.8
APAT Margin	15.6	15.8	15.1	14.0	8.3	13.6	13.0	13.7
RoE	30.6	24.2	22.9	18.7	14.8	17.9	17.3	17.2
RoCE	23.2	11.9	16.7	11.3	8.6	11.8	12.0	12.2
EFFICIENCY								
Tax Rate (%)	27.6	8.0	24.2	22.8	17.2	20.3	22.0	22.0
Fixed Asset Turnover (x)	2.6	1.6	1.8	1.1	1.2	1.3	1.3	1.4
Inventory (days)	54	70	73	75	71	68	68	68
Debtors (days)	63	88	98	110	94	85	85	85
Other Current Assets (days)	28	58	42	43	37	36	35	34
Payables (days)	66	97	94	89	82	83	81	79
Other Current Liab & Provns (days)	30	50	62	63	57	48	42	38
Cash Conversion Cycle (days)	51	61	77	95	83	70	72	74
Debt/EBITDA (x)	0.8	1.9	1.4	2.4	2.5	1.4	1.0	0.6
Net D/E (x)	0.3	0.5	0.5	0.7	0.7	0.4	0.3	0.2
Interest Coverage (x)	43.6	36.8	26.6	13.0	6.4	9.5	12.7	15.1
PER SHARE DATA (Rs)								
EPS	14.4	14.5	17.5	17.5	15.0	19.3	21.0	23.6
Dividend	3.2	3.2	3.5	3.5	7.0	7.0	7.0	7.0
Book Value	52	68	85	101	101	115	129	146
VALUATION								
P/E (x)	28.6	28.3	23.4	23.4	27.3	21.3	19.5	17.4
P/BV (x)	7.9	6.0	4.8	4.0	4.1	3.6	3.2	2.8
EV/EBITDA (x)	18.8	24.1	16.3	16.9	18.0	14.2	13.0	11.6
EV/Revenues (x)	4.5	4.9	3.9	3.8	3.5	3.1	2.9	2.6
OCF/EV (%)	4.5	2.9	2.0	2.5	5.0	6.7	5.7	6.4
FCF/EV (%)	2.3	-3.5	-0.3	0.5	3.2	5.1	3.9	4.5
Dividend Yield (%)	0.8	0.8	0.9	0.9	1.7	1.7	1.7	1.7

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
3-Nov-20	411	ADD	445

Rating Criteria

- BUY: >+15% return potential
- ADD: +5% to +15% return potential
- REDUCE: -10% to +5% return potential
- SELL: > 10% Downside return potential

Disclosure:

We, **Bansi Desai, CFA & Karan Vora, CA**, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. HSL has no material adverse disciplinary history as on the date of publication of this report. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

Research Analyst or his/her relative or HDFC Securities Ltd. **does not have** any financial interest in the subject company. Also Research Analyst or his relative or HDFC Securities Ltd. or its Associate may have beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of the Research Report. Further Research Analyst or his relative or HDFC Securities Ltd. or its associate **does not have** any material conflict of interest.

Any holding in stock –No

HDFC Securities Limited (HSL) is a SEBI Registered Research Analyst having registration no. INH000002475.

Disclaimer:

This report has been prepared by HDFC Securities Ltd and is solely for information of the recipient only. The report must not be used as a singular basis of any investment decision. The views herein are of a general nature and do not consider the risk appetite or the particular circumstances of an individual investor; readers are requested to take professional advice before investing. Nothing in this document should be construed as investment advice. Each recipient of this document should make such investigations as they deem necessary to arrive at an independent evaluation of an investment in securities of the companies referred to in this document (including merits and risks) and should consult their own advisors to determine merits and risks of such investment. The information and opinions contained herein have been compiled or arrived at, based upon information obtained in good faith from sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. Descriptions of any company or companies or their securities mentioned herein are not intended to be complete. HSL is not obliged to update this report for such changes. HSL has the right to make changes and modifications at any time.

This report is not directed to, or intended for display, downloading, printing, reproducing or for distribution to or use by, any person or entity who is a citizen or resident or located in any locality, state, country or other jurisdiction where such distribution, publication, reproduction, availability or use would be contrary to law or regulation or what would subject HSL or its affiliates to any registration or licensing requirement within such jurisdiction.

If this report is inadvertently sent or has reached any person in such country, especially, United States of America, the same should be ignored and brought to the attention of the sender. This document may not be reproduced, distributed or published in whole or in part, directly or indirectly, for any purposes or in any manner.

Foreign currencies denominated securities, wherever mentioned, are subject to exchange rate fluctuations, which could have an adverse effect on their value or price, or the income derived from them. In addition, investors in securities such as ADRs, the values of which are influenced by foreign currencies effectively assume currency risk. It should not be considered to be taken as an offer to sell or a solicitation to buy any security.

This document is not, and should not, be construed as an offer or solicitation of an offer, to buy or sell any securities or other financial instruments. This report should not be construed as an invitation or solicitation to do business with HSL. HSL may from time to time solicit from, or perform broking, or other services for, any company mentioned in this mail and/or its attachments.

HSL and its affiliated company(ies), their directors and employees may; (a) from time to time, have a long or short position in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.

HSL, its directors, analysts or employees do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of shares and bonds, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc.

HSL and other group companies, its directors, associates, employees may have various positions in any of the stocks, securities and financial instruments dealt in the report, or may make sell or purchase or other deals in these securities from time to time or may deal in other securities of the companies / organizations described in this report.

HSL or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

HSL or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction in the normal course of business.

HSL or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither HSL nor Research Analysts have any material conflict of interest at the time of publication of this report. Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions. HSL may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Research entity has not been engaged in market making activity for the subject company. Research analyst has not served as an officer, director or employee of the subject company. We have not received any compensation/benefits from the subject company or third party in connection with the Research Report.

HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066 Compliance Officer: Binkle R. Oza Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

HDFC Securities Limited, SEBI Reg. No.: NSE, BSE, MSEL, MCX: INZ000186937; AMFI Reg. No. ARN: 13549; PFRDA Reg. No. POP: 11092018; IRDA Corporate Agent License No.: CA0062; SEBI Research Analyst Reg. No.: INH000002475; SEBI Investment Adviser Reg. No.: INA000011538; CIN - U67120MH2000PLC152193

HDFC securities**Institutional Equities**

Unit No. 1602, 16th Floor, Tower A, Peninsula Business Park,

Senapati Bapat Marg, Lower Parel, Mumbai - 400 013

Board: +91-22-6171-7330 www.hdfcsec.com