

# Lupin

## Margin recovery holds the key

Lupin reported steady revenues led by good traction in India, US and API business. While margins improved (13.7%, +228bps QoQ, lower R&D spends) and recovered from Q3 lows, they still remain subdued and below our expectations. Lupin has been guiding towards an improving cost structure, however, benefits of those are yet to be seen. Going forward, we factor significant gains from operating leverage to aid margin expansion driven by key launches viz. gProAir, Levothyroxine ramp up and several cost containment measures (stable R&D, lower SG&A spends, savings on Solosec). With improving profitability and moderate capex (slightly higher than Rs5bn), we expect FCF generation of ~Rs40bn over FY20-22e. We raise our earnings by 12-18% for FY21/22 to factor slightly higher margins, lower depreciation and tax rate. Revise TP to Rs920 based on 21x FY22 EPS.

- **Q4 snapshot** – Revenues at Rs38.4bn (flat YoY, +2% QoQ, gRanexa exclusivity in the base) were driven by healthy growth in India (+13% YoY), API (+13% YoY) and US biz (USD212mn, up 14% QoQ, stable base, ramp up in Levo, some stock piling). EBIDTA Margins improved by 228bps QoQ largely on account of lower R&D (-240bps QoQ) & other exp (-55bps QoQ).
- **gProAir approval and ramp up in Levothyroxine critical for US growth:** Lupin has a rich pipeline for the US (158 pending ANDAs, 43 FTFs); however, in the near term, scale up in Levothyroxine (market share ramp up from 13% in Q4 to ~20% in FY21), ramp up in recent launches, gProAir approval (before 2HFY21) will be the key growth drivers. We expect softer trends in Solosec in FY21, although net pricing is likely to improve.
- **Multiple levers for margin expansion in place:** We expect good growth in key markets, high value launches in US coupled with several cost containment measures such as better procurement, lower SG&A spends, reduction in Solosec burn rate (annual savings of USD25mn), stable R&D exp to drive ~500bps margin expansion over the next two years.
- **Key call takeaways:** a) Guidance for FY21- EBIDTA margin of 19-20% incl other income, R&D cost – Rs15bn (flat YoY), capex – slightly higher than Rs5bn, tax rate – 35%, to further reduce in FY22; Q1FY21- to be softer; b) **Key products** – gProAir approval (before 2HFY21), gFostair approval in EU by next qtr, launch by end of FY21, Peg-filgrastim filing in US by end of FY21, gSpiriva in US – TA in FY21, launch in 2022; c) Plant remediation timeline - to invite FDA for reinspection in next 2 months for Goa followed by Indore, Somerset to precede Goa; d) Metformin NDMA issue – to recall one batch; e) Net debt - Rs15.1bn. Reduced further by ~USD267mn post March.
- **Maintain Add, risks:** We increase our TP to Rs920 based on 21x FY22e EPS. Key risks: delay in resolution of key plants, delay in key approvals, higher price erosion in the US, adverse outcome on drug price-fixing lawsuit in the US, escalation of NDMA issue in Metformin.

### Financial Summary

	Q4 FY20	Q4 FY19	YoY (%)	Q3 FY20	QoQ (%)	FY18	FY19	FY20	FY21E	FY22E
Net Sales	37,910	38,070	-0.4	37,161	2.0	158,041	144,543	152,307	165,947	184,253
EBITDA	5,253	7,793	-32.6	4,291	22.4	31,475	23,504	22,107	27,219	36,172
APAT	3,065	2,496	22.8	-5,798	na	14,718	8,521	3,526	13,999	19,860
Adj. EPS (Rs)	6.8	5.5	22.8	-12.8	na	32.5	18.8	7.8	30.9	43.8
P/E (x)						26.8	46.3	111.9	28.2	19.9
RoE (%)						10.8	6.2	2.7	9.8	12.5

Source: Company, HSIE Research

## ADD

CMP(as on 29 May 2020)	Rs 870
Target Price	Rs 920
NIFTY	9,580

KEY CHANGES	OLD	NEW
Rating	ADD	ADD
Price Target	Rs 720	Rs 920
EPS %	FY21E 12%	FY22E 18%

### KEY STOCK DATA

Bloomberg code	LPC IN
No. of Shares (mn)	453
MCap (Rs bn) / (\$ mn)	394/5,214
6m avg traded value (Rs mn)	2,046
52 Week high / low	Rs 919/505

### STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	15.6	45.5	70.2
Relative (%)	39.6	70.6	92.6

### SHAREHOLDING PATTERN (%)

	Dec-19	Mar-20
Promoters	46.93	46.92
FIs & Local MFs	13.42	16.27
FPIs	24.66	22.68
Public & Others	14.99	14.13
Pledged Shares	0.00	0.00

Source : BSE

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Revenues were largely in line with the estimates.

Gross margins decreased by ~611bps YoY and 47bps QoQ on account of Ranexa exclusivity in the base

R&D spend was lower at 9% of sales (~10.2% of sales in FY20)

Other expenditure declined by 55 on a QoQ basis

EBITDA margin increased by 228bps QOQ to 13.7% as lower gross margins were offset by lower R&D and other expenses

Depreciation cost in Q4 - new base

EO items include profit on divestment of Kyowa and impairment of intangibles

Forex gain – Rs1.26bn in Q4

Tax rate will reduce to ~35% in FY21 and further down in FY22

India growth (+13% YoY) outperformed the 9.7% growth of IPM for the quarter

US biz (+14% QoQ) was driven by stable base, Levo ramp up and some stock piling in March

EMEA grew by 7% led by strong growth in South Africa

### Quarterly Financial Snapshot

Rs mn	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
Net Sales	38,457	38,866	(1.1)	37,693	2.0	152,307	144,543	5.4
EBITDA	5,253	7,793	(32.6)	4,291	22.4	22,107	23,504	(5.9)
Other income	2,086	733	184.7	936	122.9	6,279	5,433	15.6
Depreciation	2,143	2,191	(2.2)	2,532	(15.4)	9,702	8,461	14.7
Interest	1,074	843	27.4	886	21.2	3,630	3,025	20.0
<b>PBT</b>	<b>4,123</b>	<b>5,492</b>	<b>(24.9)</b>	<b>1,809</b>	<b>128.0</b>	<b>8,834</b>	<b>14,997</b>	<b>(41.1)</b>
Tax	1,051	2,943	(64.3)	7,670	(86.3)	11,571	8,879	30.3
Minority	7	53	(87.4)	(64)	(110.5)	(43)	52	(183.6)
<b>Adjusted PAT</b>	<b>3,065</b>	<b>2,496</b>	<b>22.8</b>	<b>(5,798)</b>	<b>(152.9)</b>	<b>3,526</b>	<b>8,521</b>	<b>(58.6)</b>
Extra ordinary income/ (exp.)	(831)	(400)	107.8	2,552	(132.6)	6,220	2,455	153.3
<b>Reported PAT</b>	<b>3,896</b>	<b>2,896</b>	<b>34.6</b>	<b>(8,350)</b>	<b>(146.7)</b>	<b>(2,694)</b>	<b>6,066</b>	<b>(144.4)</b>

Source: Company, HSIE Research

### Margin Analysis

	Q4FY20	Q4FY19	YoY (bps)	Q3FY20	QoQ (bps)	FY20	FY19	YoY (bps)
Material Expenses % Net Sales	36.5	30.4	611.0	36.1	47.0	35.7	34.2	143.7
Employee Expenses % Net Sales	19.9	18.2	163.4	19.7	20.3	19.6	19.2	44.6
R&D Expenses % Net Sales	9.0	10.2	(124.6)	11.3	(239.7)	10.2	10.9	(68.2)
Other Expenses % Net Sales	21.0	21.1	(10.8)	21.6	(55.2)	20.0	19.5	54.5
EBITDA Margin (%)	13.7	20.0	(639.0)	11.4	227.6	14.5	16.3	(174.6)
Tax Rate (%)	25.5	53.6	(2,809.8)	424.1	(39,861.1)	76.9	50.9	na
APAT Margin (%)	8.0	6.4	154.9	-15.4	2,335.3	2.3	5.9	(358.0)

Source: Company, HSIE Research

### Segmental Quarterly Performance

Rs mn	Q4FY20	Q4FY19	YoY (%)	Q3FY20	QoQ (%)	FY20	FY19	YoY (%)
India	11,920	10,525	13.3	12,969	-8.1	51,385	46,382	10.8
US	15,791	17,406	-9.3	13,766	14.7	58,212	55,924	4.1
APAC	1,447	1,712	-15.5	1,722	-16.0	6,069	5,600	8.4
EMEA	3,650	3,397	7.4	2,913	25.3	12,364	11,906	3.8
LatAm	1,353	1,385	-2.3	1,796	-24.7	6,143	5,658	8.6
ROW	463	733	-36.8	822	-43.7	2,815	2,143	31.4
Formulations	34,624	35,158	-1.5	33,988	1.9	136,988	127,613	7.3
API	3,286	2,912	12.8	3,173	3.6	12,999	13,464	-3.5
other operating income	547	796	-31.2	532	2.9	2,320	3,465	-33.1
<b>Total</b>	<b>38,457</b>	<b>38,866</b>	<b>-1.1</b>	<b>37,693</b>	<b>2.0</b>	<b>152,307</b>	<b>144,542</b>	<b>5.4</b>

Source: Company, HSIE Research

### Revise TP to Rs920, Maintain Add

We increase our earnings estimates by 12-18% for FY21-22e as we factor slightly higher margins and lower depreciation & tax rate as guided by the management. We increase our target multiple to 21x (from 19x earlier) in line with sector average. Our revised TP of Rs920 is based on 21x FY22 EPS. We maintain Add rating on the stock.

# Financials

## Income Statement

Year to March (INR mn)	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
<b>Revenues</b>	<b>127,700</b>	<b>142,018</b>	<b>174,940</b>	<b>158,041</b>	<b>144,543</b>	<b>152,307</b>	<b>165,947</b>	<b>184,253</b>
Material Cost	52,158	55,747	65,978	67,081	62,624	68,114	73,823	78,988
Gross Margins (%)	59.2	60.7	62.3	57.6	56.7	55.3	55.5	57.1
Personnel cost	17,473	21,077	28,495	28,647	27,702	29,868	31,530	33,629
Selling expenses	10,303	11,531	13,297	9,737	10,969	11,506	11,920	12,666
Administrative expenses	11,570	16,196	22,242	21,101	19,744	20,711	21,455	22,799
<b>EBITDA</b>	<b>36,195</b>	<b>37,468</b>	<b>44,928</b>	<b>31,475</b>	<b>23,504</b>	<b>22,107</b>	<b>27,219</b>	<b>36,172</b>
EBITDA Margins (%)	28.3	26.4	25.7	19.9	16.3	14.5	16.4	19.6
Depreciation	4,347	4,635	9,122	10,859	8,461	9,702	7,809	8,297
Interest	98	447	1,525	2,044	3,025	3,630	1,933	1,093
Other Income	2,398	1,877	1,065	1,504	5,433	6,279	3,990	3,238
PBT before EO items	34,148	34,263	35,346	20,076	17,452	15,054	21,467	30,019
Extra-ordinary (Income) / Exps	-	-	1,559	12,206	2,455	6,220	-	-
PBT after EO items	34,148	34,263	33,787	7,870	14,997	8,834	21,467	30,019
Tax	9,704	11,535	9,785	5,322	8,879	11,571	7,513	10,206
PAT	24,444	22,728	24,002	2,548	6,117	-2,737	13,953	19,813
<b>Adjusted Net income</b>	<b>24,032</b>	<b>22,867</b>	<b>25,140</b>	<b>14,718</b>	<b>8,521</b>	<b>3,526</b>	<b>13,999</b>	<b>19,860</b>

Source: Company, HSIE Research

## Balance Sheet

Year to March (INR mn)	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
<b>Shareholders Funds</b>	<b>88,741</b>	<b>111,634</b>	<b>134,976</b>	<b>135,770</b>	<b>137,422</b>	<b>131,464</b>	<b>142,198</b>	<b>158,794</b>
Share Capital	899	901	903	904	905	906	906	906
Reserves & Surplus	87,842	110,733	134,073	134,865	136,517	130,558	141,292	157,888
Secured Loans	970	3,241	1,908	6,965	4,462	4,462	4,462	4,462
Unsecured Loans	4,402	68,534	77,753	64,463	80,500	43,206	23,206	15,206
Other Long Term Liabilities	441	4,777	6,032	5,258	7,296	7,296	7,296	7,296
Total Loans	5,812	76,552	85,693	76,686	92,258	54,964	34,964	26,964
Deferred tax liabilities	2,024	3,267	3,949	2,855	2,883	2,883	2,883	2,883
Minority Interest	241	321	345	401	469	425	380	332
<b>Total Liabilities</b>	<b>96,818</b>	<b>191,773</b>	<b>224,963</b>	<b>215,712</b>	<b>233,031</b>	<b>189,736</b>	<b>180,424</b>	<b>188,972</b>
Fixed Assets	27,201	64,515	87,229	79,135	87,064	35,362	33,652	31,455
C-WIP	5,760	27,024	21,331	25,982	16,397	27,374	27,374	27,374
Investments	25	143	220	267	1,856	1,856	1,856	1,856
Deffered Tax Asset	842	3,359	5,076	7,166	7,340	7,340	7,340	7,340
Goodwill on Consolidation	16,481	22,654	23,100	24,485	23,803	17,803	17,803	17,803
Current Investments	16,559	20	21,141	2,349	21,099	23,000	15,000	15,000
Inventories	25,036	32,737	36,423	36,625	38,368	32,463	35,394	42,320
Sundry Debtors	26,569	45,488	43,073	51,964	51,498	51,365	56,002	54,768
Cash & Bank Balance	4,814	8,218	6,994	14,080	9,872	20,436	16,632	26,022
Loans & Advances	6,163	18,061	17,180	15,682	14,936	16,501	17,702	19,022
Other Current Assets	1,929	4,030	4,305	5,319	7,262	7,262	7,262	7,262
Current Assets	81,069	108,553	129,117	126,018	143,033	151,027	147,991	164,393
Current Liabilities	27,197	28,288	31,413	35,916	33,567	39,150	42,936	48,363
Provisions	7,363	6,187	9,697	11,425	12,895	11,876	12,656	12,887
Net Current Assets	46,509	74,078	88,006	78,677	96,571	100,001	92,399	103,144
<b>Total Assets</b>	<b>96,818</b>	<b>191,773</b>	<b>224,963</b>	<b>215,712</b>	<b>233,031</b>	<b>189,736</b>	<b>180,424</b>	<b>188,972</b>

Source: Company, HSIE Research

## Cash Flows

Year to March (INR mn)	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
<b>PBT</b>	34,148	33,288	35,431	5,468	15,172	15,054	21,467	30,019
Depreciation and Amortisation	4,347	4,871	9,122	10,859	8,461	9,702	7,809	8,297
Interest and Finance Charges	98	595	1,525	2,044	3,025	3,630	1,933	1,093
Change in Working Capital	-949	-23,089	3,358	-8,992	-5,132	9,035	-4,202	-1,355
Direct Taxes Paid	-9,436	-11,701	-11,490	-5,584	-9,394	-11,571	-7,513	-10,206
<b>Operating Cash Flows</b>	<b>27,331</b>	<b>4,401</b>	<b>39,529</b>	<b>30,956</b>	<b>16,579</b>	<b>19,630</b>	<b>19,494</b>	<b>27,848</b>
Change in Fixed Assets	-8,676	-57,815	-26,007	-14,898	-9,599	37,023	-6,100	-6,100
Change in Investments	3,699	13	121	19,189	-24,268	-1,901	8,000	-
<b>Investing Cash Flows</b>	<b>-10,545</b>	<b>-69,617</b>	<b>-25,287</b>	<b>4,699</b>	<b>-32,825</b>	<b>35,122</b>	<b>1,900</b>	<b>-6,100</b>
Proceeds from (Repayment of) Borrowings	-700	62,081	9,479	-8,953	12,922	-37,294	-20,000	-8,000
Issue of Equity Shares	2	2	2	1	1	1	-	-
Interest paid	-109	-585	-1,507	-2,040	-2,804	-3,630	-1,933	-1,093
Dividend Paid	-1,573	-4,055	-4,066	-4,073	-2,713	-3,265	-3,265	-3,265
<b>Financing Cash Flows</b>	<b>-1,969</b>	<b>58,364</b>	<b>4,332</b>	<b>-14,921</b>	<b>7,441</b>	<b>-44,188</b>	<b>-25,198</b>	<b>-12,358</b>
Net Change in Cash	14,817	-6,852	18,574	20,733	-8,804	10,564	-3,804	9,390
Opening cash balance	6,066	20,951	7,802	6,875	14,164	9,872	20,436	16,632
<b>Closing cash balance</b>	<b>21,084</b>	<b>16,028</b>	<b>26,376</b>	<b>27,608</b>	<b>5,360</b>	<b>20,436</b>	<b>16,632</b>	<b>26,022</b>

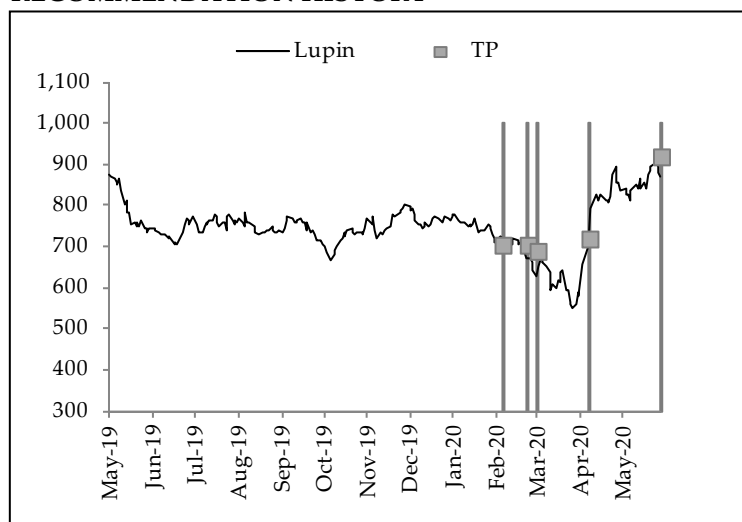
Source: Company, HSIE Research

## Key Ratios

Year to March	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E	FY22E
<b>PROFITABILITY (%)</b>								
GPM	61.0	63.0	63.6	58.5	58.1	56.1	56.3	57.9
EBITDA Margin	28.3	26.4	25.7	19.9	16.3	14.5	16.4	19.6
APAT Margin	19.4	16.7	14.7	9.5	6.0	2.4	8.6	10.9
RoE	27.1	20.5	18.6	10.8	6.2	2.7	9.8	12.5
RoIC (or Core RoCE)	27.9	15.8	12.9	7.2	3.5	1.5	7.6	11.3
RoCE	25.3	12.0	11.9	7.5	4.3	2.3	8.4	10.9
<b>EFFICIENCY</b>								
Tax Rate (%)	28.4	33.7	27.7	26.5	50.9	76.9	35.0	34.0
Fixed Asset Turnover (x)	2.5	2.0	1.7	1.4	1.1	1.6	1.7	1.8
Inventory (days)	74	87	78	86	99	79	79	85
Debtors (days)	78	121	92	122	133	125	125	110
Other Current Assets (days)	6	11	9	12	19	18	16	15
Payables (days)	58	53	55	60	65	56	55	55
Other Current Liab & Provns (days)	41	35	26	49	53	75	74	72
Cash Conversion Cycle (days)	94	155	114	147	168	148	149	140
Debt/EBITDA (x)	0.0	1.8	1.8	2.0	3.5	1.6	0.7	0.0
Net D/E (x)	0.0	0.6	0.6	0.5	0.6	0.3	0.1	0.0
Interest Coverage (x)	324.7	73.5	23.5	10.1	5.0	3.4	10.0	25.5
<b>PER SHARE DATA (Rs)</b>								
EPS	53.2	50.6	55.5	32.5	18.8	7.8	30.9	43.8
Dividend	3.5	9.0	9.0	9.0	6.0	7.2	7.2	7.2
Book Value	196.3	246.9	298.0	299.5	303.1	290.0	313.7	350.3
<b>VALUATION</b>								
P/E (x)	16.4	17.2	15.7	26.8	46.3	111.9	28.2	19.9
P/BV (x)	4.4	3.5	2.9	2.9	2.9	3.0	2.8	2.5
EV/EBITDA (x)	10.8	12.3	10.5	14.5	20.2	19.4	15.1	10.9
EV/Revenues (x)	3.1	3.3	2.7	3.0	3.4	2.9	2.6	2.3
OCF/EV (%)	6.9	-0.8	8.7	6.5	3.5	4.6	4.7	7.0
FCF/EV (%)	4.7	-13.4	3.1	0.4	0.9	14.7	3.2	5.5
FCFE/Mkt Cap (%)	4.6	0.2	6.5	-1.3	5.1	7.4	-1.2	3.8
Dividend Yield (%)	0.4	1.0	1.0	1.0	0.7	0.8	0.8	0.8

Source: Company, HSIE Research

## RECOMMENDATION HISTORY



Date	CMP	Reco	Target
7-Feb-20	721	NEU	705
24-Feb-20	699	NEU	705
2-Mar-20	640	ADD	690
8-Apr-20	700	ADD	720
01-Jun-20	870	ADD	920

From 2<sup>nd</sup> March 2020, we have moved to new rating system

## Rating Criteria

BUY: >+15% return potential

ADD: +5% to +15% return potential

REDUCE: -10% to +5% return potential

SELL: > 10% Downside return potential

**Disclosure:**

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