

INITIATING COVERAGE

CMP: ₹547/-

7th March 2019

BUY

SECTOR: Pharmaceuticals

Cipla Limited



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Company Details

Key Stock Data

CMP	547
Market Cap (₹ Crs)	44,031.45
52W High/Low	678.45 / 483.75

Bloomberg	CIPLA IN
NSE Code	CIPLA
BSE Code	500087

Shareholding Pattern in %

Promoters	36.70
Public & Others	63.30

We initiate coverage on Cipla with **BUY** rating. Our investment thesis is backed by

- Domestic pharma market will continue to report volume growth,
- Global generic respiratory products opportunities remain untapped,
- US market hurdles are behind and
- Outperformance by Cipla in African private market.

Cipla is the third largest player in the domestic market with a market share of 4.7%. It has built a strong domestic franchise with leadership in the respiratory segment and is currently expanding its footprint in the US. We expect Cipla to clock revenue CAGR of 8.5% over FY18-20E, and report EBITDA margin of 18.67% and 19.54% in FY19E and FY20E. **At the CMP of 547, Cipla is currently trading at 30x FY19E P/E and 23x FY20E P/E.** However, the valuation and our estimated earnings do not incorporate the adverse risk outcome of the pharma regulators which can delay monetization of respiratory product pipeline and key launches in the US and other markets.

Key Financial Highlights

(₹Cr)

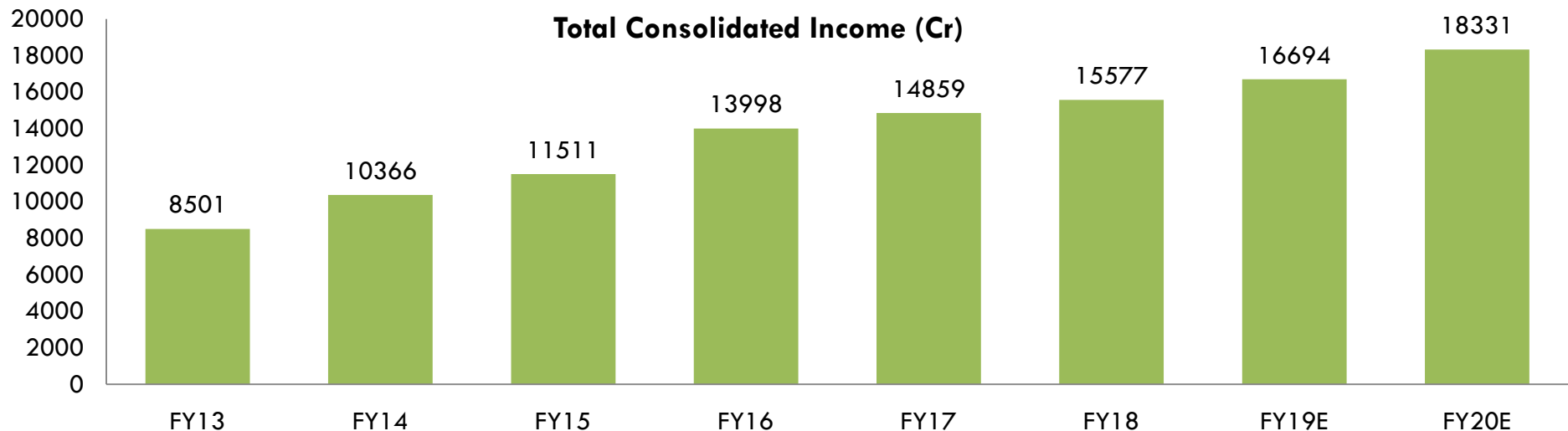
	FY16	FY17	FY 18	FY19E	FY 20E
Total Income	13998	14859	15577	16694	18331
Total Expense	12271	13637	13830	14671	15648
Profit Before Tax	1727	1222	1747	2023	2682
EBITDA	2481	2476	2831	3050	3513
Net Profit	1395	1042	1497	1457	1931
EPS	17.17	12.51	17.51	18.08	23.96

Source : Company , Way2Wealth Research

Company Background

Cipla was founded by Khwaja Abdul Hamied as 'The Chemical, Industrial & Pharmaceutical Laboratories' in 1935 in Mumbai. In 1960, Dr. Hamied joined Cipla Ltd. as an officer-in-charge of research and development.

Cipla, under Yusuf's leadership, achieved several milestones and changed the face of Indian Pharma Industry. One of the greatest achievement under Yusuf's leadership was to initiate offering of the triple-drug cocktail, Triomune that helps in fighting against HIV and AIDS at prices lower than those available internationally. Cipla is amongst the world's largest producers of low-cost antiretroviral drugs for AIDS. The company's manufacturing facilities are spread over seven locations including Goa, Bengaluru, Baddi, Indore, Kurkumbh, Patalganga, and Sikkim. Cipla offers one of the world's largest portfolio of inhalation products, with 27 molecules and combinations across a range of devices which cater to diversified patient needs. The Company has five manufacturing facilities dedicated to respiratory products.



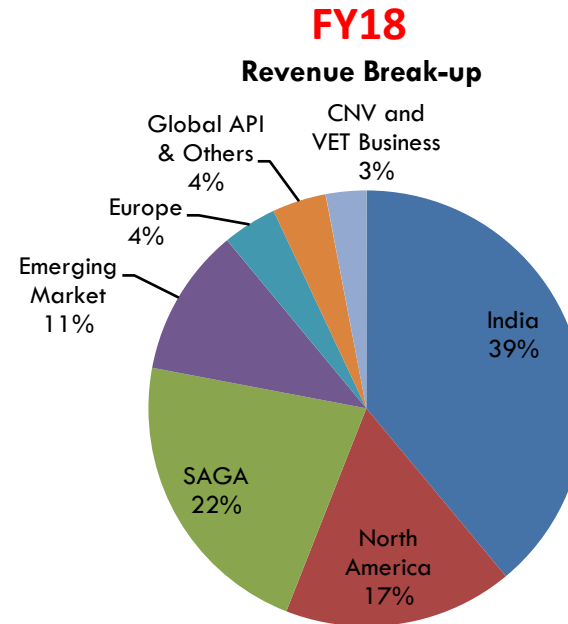
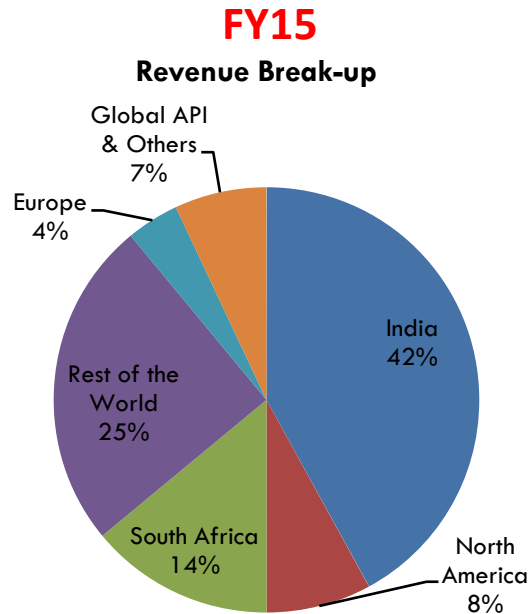
Source : Company Reports and Way2Wealth Research

Cipla is the third largest player in India and this region contributes about 39% to the consolidated revenues. The company has become the biggest player in the domestic market in the respiratory segment and is on its path replicating the same in other markets. Cipla has been a late entrant in the US market. The company marked its presence in the US market through the acquisition of InvaGen and Exelan Pharmaceuticals in the year 2013. The acquisition helped Cipla to set up its own front-end unit in the US market and expand its products offering. Unlike its peers, Cipla still doesn't have a significant presence in the US market. It only generates 17% of consolidated revenue. Currently, the company has about 68 ANDAs (Cipla 40, InvaGen 22, partnered 4, and PEPFAR 2) pending approval in the US and going forward a large portion of the company's growth is expected to be driven by US business. South Africa stands out to be an important market for Cipla. Cipla earlier used to sell products through its channel partner Medpro, but later it went to acquire its front-end partner Medpro.

Key acquisition made by Cipla

Target Co Name	Amount Paid	Date	Country	Details
InvaGen and Exelan	\$550Mn. \$500Mn for InvaGen and \$50 Mn for Exelan. (₹3,650 Cr)	Sept-2015	US	The acquisition of InvaGen pharmaceuticals provided Cipla with about 40 approved ANDAs, 32 marketed products, and 30 pipeline products. In addition, InvaGen had filed 5 first-to-file products. InvaGen has 3 units located in Long Island, NY, with a total production capacity of 12 billion tablets and capsules per annum and about 500 employees.
Medpro	\$512 Mn. (₹2,707 Cr)	July, 2013	Africa	Cipla was the biggest supplier of drugs to Cipla Medpro. The group's operations include two divisions. One is Cape Town-based Cipla Medpro which is into an extensive range of chronic care medicines and OTC products. The other is Cipla Medpro Manufacturing.

Cipla expanded its presence in the US market



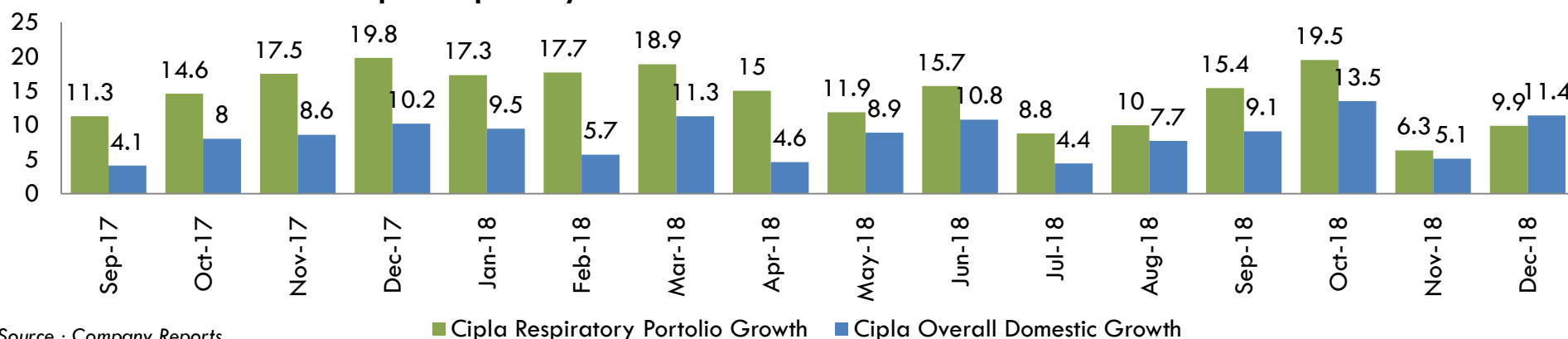
Cipla has been growing its presence in 52 countries including 13 countries via a direct-to-market model. The Company is focusing on deepening its presence in Australia, Colombia, China, Brazil, and Indonesia through a combination of in-house pipeline products and partnerships. The company has few products that are in the development stage for China and Brazil. These filings, approvals, and partnerships module will help in driving significant growth in emerging markets over the medium and long-term.

Investment Rationale

Cipla to maintain its leadership in domestic respiratory market

Cipla over the years has focused on building a strong domestic respiratory portfolio and has achieved the leadership position in the segment with 67% market share in inhalation segment, and the company expects a potential for a 14-15 % growth as the market is under-penetrated. Cipla has strongly captured most of the market with its successful brands like Foracort, Duolin, and Budecort. It generates 39% of its consolidated revenue from domestic markets with respiratory therapy contributing nearly 34% of its domestic sales. Cipla has nearly 70 respiratory products to offer in the domestic market. The company's dominance in the respiratory space is mainly due to broad marketing and distribution reach. The respiratory products offer high margins and are difficult to develop because of the complexity. We believe, the opportunity in the respiratory segment is still huge in India as there are an estimated 90 million patients with respiratory illnesses and only less than 10 million get proper treatment. While inhalers have proven to be safer and efficient compared with oral form, we expect the demand to increase for inhaler products, if proper awareness is created among patients to shift from an oral form dosage to inhalers. In India, only 30 % of patients take inhalers in India, compared to 70 % globally. Cipla is making its efforts through the "BreatheFree" patient awareness and education programs across markets to provide support for respiratory care.

Cipla Respiratory Products & Domestic Portfolio Growth Y-o-Y in %

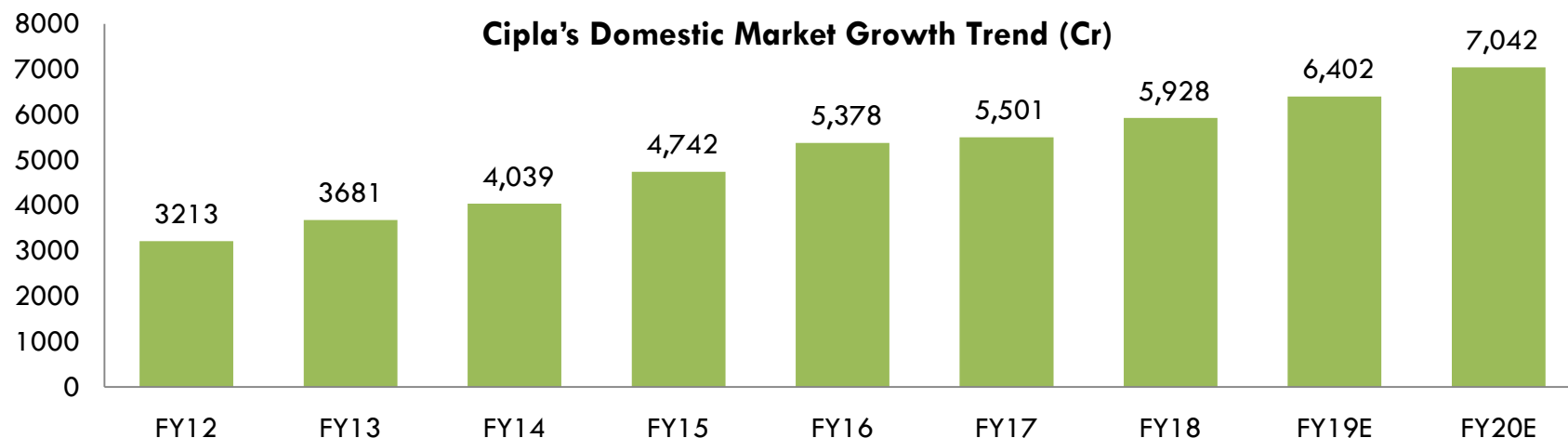


Source : Company Reports

Marketing and sales force productivity to drive growth in domestic market

Cipla has a market share of 4.6% in domestic market and the company has been able to build a very strong domestic business in the last few years by nearly doubling its Indian sales from ₹3213Cr in FY12 to ₹5928Cr in FY18. It generates around 40% of its sales from the domestic business and most of it is contributed by respiratory and Anti-Infectives therapy. The domestic revenue has grown at a CAGR of 13% over the past 6 years, above industry growth of 10.3%. In FY18, India business registered a 11% growth over last year backed by 22 product launches and above-market growth for all key therapies last year with cardiology reporting 9% growth (market growth of 6%), respiratory reporting 10% growth (market growth of 8%) and urology 11% (market growth of 10%).

Cipla has set a very optimistic target for its domestic business of revenues to reach ~\$1bn in FY19, which we believe can be achieved by volume growth, new launches and focus on diabetes and respiratory therapies. We expect Cipla to continue its growth momentum in the domestic business aided by new products launches and improving sales force productivity.



Source : Company Reports

Domestic pharma companies well placed over MNCs to capture Indian story

We prefer domestic pharmaceutical companies over MNCs because of the strength of the distribution network, focus on new launches, lesser dependence on single brands and lesser exposed to pricing risk. Indian market success has been predominantly due to an increase in volume because of the productivity of medical representatives and distribution reach in Tier- II and Tier –III cities. The business strategy of domestic companies is to focus on diversified therapy and brands and are better placed than MNC companies which have highly fragmented drug portfolio. The top 5 drugs contribute almost 33-40% of total revenue for MNC companies while the contribution from top 5 drugs is only in the range of 10-17% for their domestic counterparts.

Contribution to domestic revenue from Top 5 Brands

Domestic Companies	
Sunpharma	10.89%
Cipla	17.64%
Lupin	10.83%
Dr Reddy	17.31%
Mankind	12.79%

Multinational Companies	
GSK Pharma	33.06%
Sanofi India	37.33%
Abbott India	20.56%
Pfizer	29.00%
Merck	39.43%

Source : Company Reports

Competitive pricing of domestic players to have an edge over MNCs

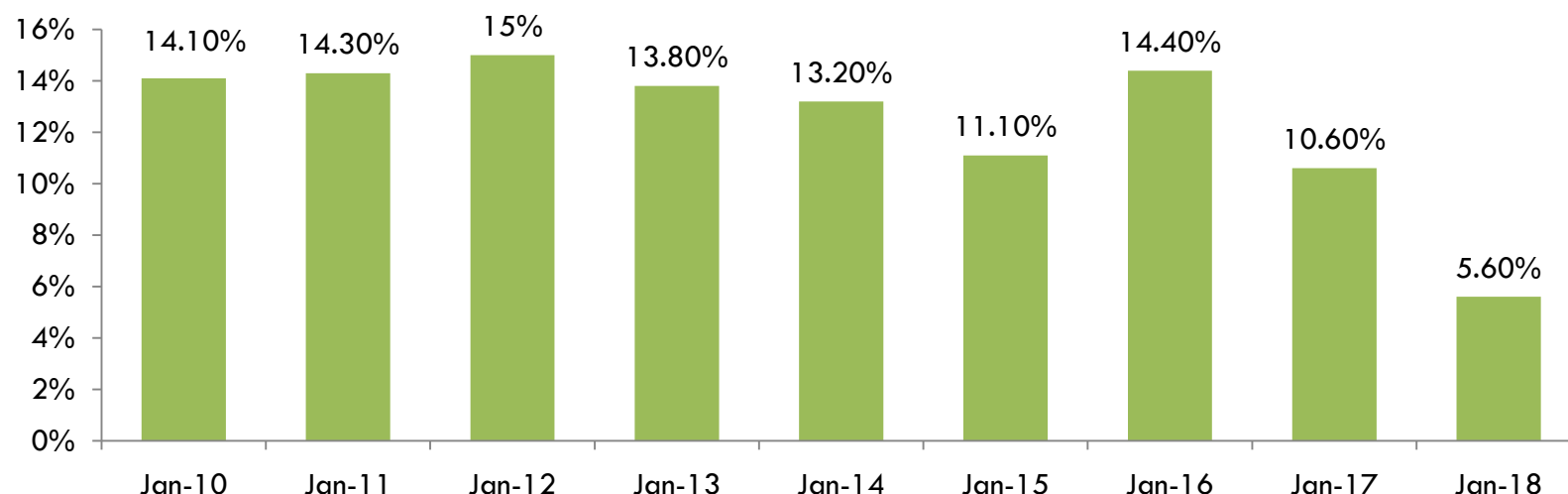
We believe domestic companies pricing strategy is better placed over MNCs due to the number of new launches by partnering and licensing strategies and winning patent cases over Multinationals. MNCs usually price their drugs at premiums comparing with domestic pharmaceutical companies. The price difference between a domestic company product and its MNC substitute is usually 2x or 3x and sometime beyond that. We believe there is a significant risk to MNCs because of their premium pricing policy, as the government aims to provide affordable medicines, and we believe price erosion can be significant.

Salt Name	Brand Name	MNC Company	Price	Substitute	Substitute Price	Price Difference
Amoxycillin 500mg + Clavulanic acid 125mg	Augmentin	GSK Pharma	260	Cipla	88	2.95x
				Glenmark	96	2.70x
				Mankind	75	3.46x
Chlorpheniramine (4mg) + Codeine (10mg)	Phensedyl Cough Linctus	Abbott India	106	Alembic Pharma	55	1.92x
				Cadila	48	2.20x
				Glenmark	29	3.65x
Piroxicam (20mg)	Dolonex Rapid	Pfizer Ltd	124	Cipla	51	2.43x
				Zydus Cadila	24	5.16x
				Sun Pharma	32	3.87x

Domestic pharma market on a firm footing; growth to persist

Indian domestic pharma market has recorded growth each year in last several years in spite of the changing industry dynamics in the face of GST, demonetization, an extension of NLEM (National List of Essential Medicine) and push towards promoting unbranded generics. Although the speed of growth has moderated in the last few years due to implementation of GST and price control measures getting more stringent, we believe that the domestic market growth story will continue its growth path supported by factors like an increasing number of Indians favoring OTC drugs, rising income levels, improving health infrastructure and improving lifestyle with health insurance.

Indian Domestic Market Growth Rate

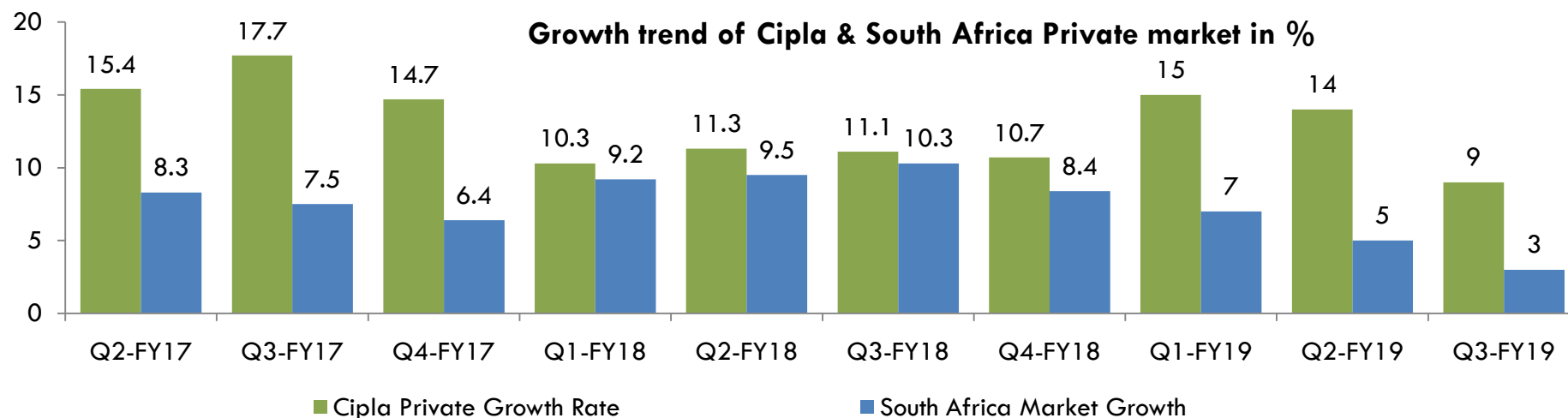


SAGA region (South Africa Private market + Cipla Global Access)

SAGA region is Cipla's second largest market contributing 22% to the consolidated sales. Cipla has been present in South Africa since last 2 decades but in the last few years, they have made their presence stronger by entering front-end market by acquiring Medpro in 2013 and JV with Teva to expand its product portfolio.

South Africa private market

Cipla acquired Medpro in the year 2013 for \$512Mn. Prior to the acquisition, Medpro was Cipla's distribution partner in South Africa. Post-acquisition Cipla's market share in South Africa stands at 5 % with Aspen and Adcock dominating the drug market in Africa. In 2014, Cipla entered into a JV with Teva where Cipla will exclusively market Teva's pharmaceutical product portfolio in South Africa. This JV has helped Cipla significantly broaden its portfolio offering to a number of therapeutic areas such as oncology, cardiovascular, CNS, and Over-The-Counter products. Cipla is the 4th largest private market player in Africa and among the fastest growing companies there.



Source : Company Reports

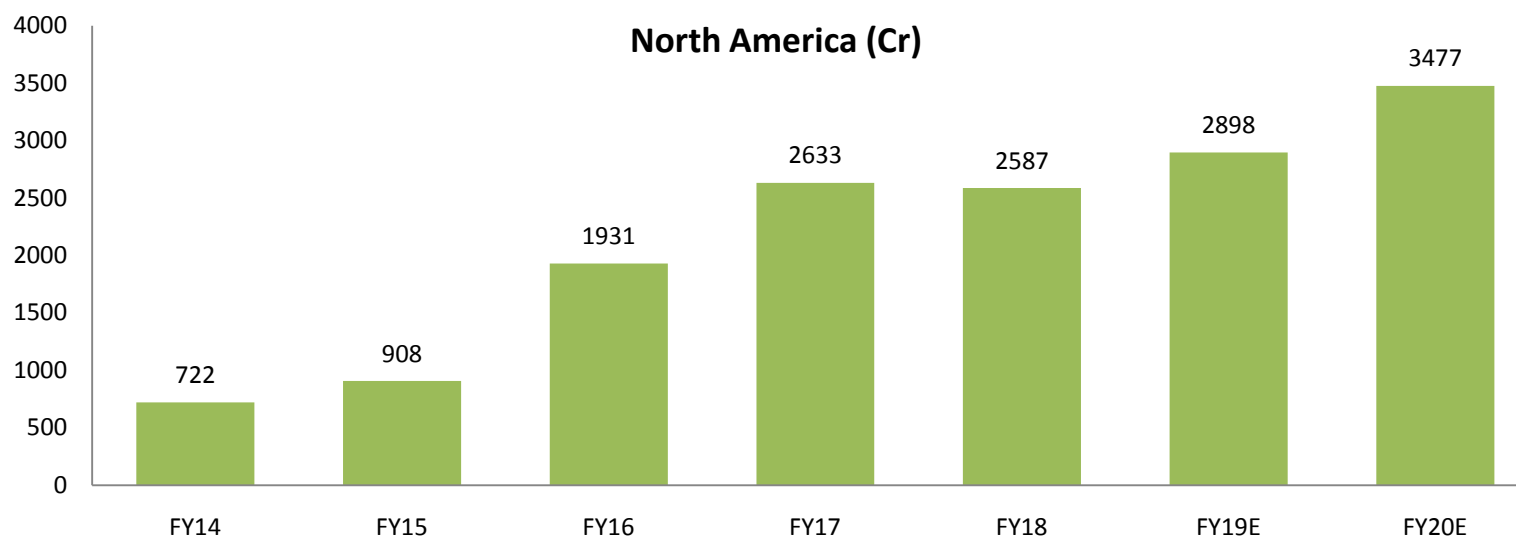
Generic Inhalers opportunity in the US market still remains untapped

The global respiratory market was about USD15.14Bn in 2016 with North America accounting for the largest share followed by Europe, Asia-Pacific, and RoW. Majority of the US respiratory inhaler products are still under patent protection while generic products enjoy only a small share in the overall pie. The inhaler market is primarily dominated by only a few players like Teva, Astrazeneca, Glaxosmithkine, Merck and Boehringer Ingelheim due to the large development cost, high chances of failure of trials and requirement of experienced professionals for the development of these products. We expect Cipla to benefit from the launch of generic inhaler products in the first wave which would help to capture relevant market share. Cipla plans to launch one Inhaler product every year in the US starting from Albuterol in FY20 and Advair in FY21 and sees \$100Mn revenue from each of the key products.

Inhaler	Market Size	Details
Advair	\$4.20 Bn	Advair is one of the important product in inhalers segment with a sales of ~\$4.2 bn. Advair patent expired in 2016 but GSK continued to be the sole seller for few years. Recently, Mylan has launched Advair at 70% discount while other players have either received CRL or are in the early stage of development. Cipla has initiated the clinical trial for Advair and is expected to file for the product in FY20 and Lupin is also in a race for the same. With Advair one of the top-selling products in the US, its opportunity remains huge for Cipla if it is able to launch the product early and capture market share. Cipla has already launched Advair in European countries with its brand name Serroflo.
Nasonex	\$600 Mn	Nasonex patent expired in 2018. Generic has been launched in the US by Apotex while Cipla may launch Nasonex in the US. Cipla already holds approval for Nasonex generic in Europe.
Albuterol	\$1.20 Bn	Cipla has already filed for the Albuterol in the US and received CRLs from the regulator. We expect the launch to be in FY20.
Symbicort	\$1.52 Bn	Currently, AstraZenca is the only player in the market selling Symbicort. We expect Cipla to pursue for Symbicort once its patent/exclusivity expires.
Dulera	\$300Mn	Currently Merck Sharp Dohme sells this product and we expect Cipla to pursue for dulera once its patent expires in 2020.
Breo Ellipta	\$1.2 Bn	Breo is a patented product of Glaxo. Cipla can be a potential filler once its patent expires in 2020-21.

Launch of limited competition generic drug in the US to help expand its footprint in the region

Cipla's exposure to the US market in early years was limited since it adopted a conservative approach by adopting a B2B model, where they used to partner with companies and sell their products. But after the acquisition of Invagen and Exelan in 2015, Cipla expanded its footprint in the US by offering a wide range of products directly in the market. The acquisition of InvaGen pharmaceuticals provided Cipla with about 40 approved ANDAs, 32 marketed products, and 30 pipeline products which are expected to be approved over the next 4 years. In the current scenario, 70% business is from direct-to-market with Invagen and Cipla's own front-end filings in the United States. Cipla's own front-end filings and B2B enjoys a higher margin compared to Invagen products that are highly commoditized in nature. We expect Cipla's US business to report a growth of 12% in FY19 and 20% in FY20 with most of the incremental growth coming from its own front end filings.



Source : Company Reports and Way2Wealth Research

The recent limited competition launches from Cipla like Renvela, Dacogen, Aloxi, and Pulmicort have aided growth in the US over the last few quarters. However, Dacogen and Pulmicort launch were not ramped up to the mark due to supply issues in the US facility and product recall. The management expects further ramp-up during the year for Dacogen before it settles at a fair market share. With new launches in the US coming mainly from its own front end, we expect margins of Cipla to improve going forward. Cipla is expected to launch one limited competition generic each quarter and file 20-plus new filings for the full year which will allow expensing more in R&D to conduct inhalers trials. We believe successful limited competition launches and ramp up in the US market going ahead will be the key triggers for Cipla.

Recent Limited competition Launches

API Name	Innovator Brand Name	Market Size	Launch Date
Sevelamer Carbonate Tablets, 800	Renvela	\$1.85Bn	Oct 27, 2017
(Palonosetron HCl Injection 0.25 mg/5 ml	Aloxi	\$460Mn	Mar 26, 2018
Budesonide Inhalation	Pulmicort	\$825Mn	Nov 16, 2017
Decitabine	Dacogen	\$180Mn	Nov 16, 2017
Testosterone Cypionate Injection	DepoTestosterone	\$191Mn	June 21, 2018
Isoproterenol Hydrochloride Injection	Isuprel Injection	\$148Mn	June 13, 2018
Diclofenac	Voltaren	\$353Mn	Aug 3, 2018
Atazanavir	Reyataz	\$324M	Aug 10, 2018
Medroxyprogesterone Injectable	Depo-Provera	\$159Mn	Jan 28, 2019

On a path of turning a family run business into professional managed company

Cipla was founded by Khwaja Abdul Hamied as 'The Chemical, Industrial & Pharmaceutical Laboratories' in 1935 in Mumbai and later name of the company was changed to 'Cipla Limited' on 20 July 1984. Yusuf K Hamied took over Cipla after the death of his father Khwaja Abdul Hamied in 1972 when Cipla's revenue was ₹1.66 Cr. However, after his retirement in 2013, the company had crossed revenue of ₹8000 Cr. Yusuf's focus stayed on volume growth and low-cost strategy ensuring that pharmaceuticals are accessible and affordable to all. Cipla was known as one of the of the best family-run companies in the country but after Yusuf Hamied's retirement in 2013 as MD, Cipla has been in the process to make it a professionally managed company. The company hired several professionals at management level after Y.K. Hamied stepped down as Managing Director in Feb-2013

Cipla hired Umang Vohra as the Managing Director & Global Chief Executive Officer in 2016. The company has done major restructuring to stay focused on core respiratory business and increase its presence in the US. In the past few years, Cipla exited many countries, including the front-end business in European countries. The company decided not to remain an active player in the biosimilar spaces as they believed that much more efficient players are present in this space and biosimilars business will become more competitive. We expect Cipla to focus on respiratory business and increase its presence in the US going ahead.

List of Cipla's exit from non-core and low profit businesses :

- Sold its animal health business in South Africa to Ascendis Health Ltd for 375 Mn rand (about ₹192 Cr) in March 2017.
- Divested 16.7 % stake in Chase Pharmaceuticals Corporation.
- Exited Croatian subsidiary to PharmaS for \$1.1 million (₹7 Cr)
- MOU opted out to set up biosimilar plant in Africa plant.
- Exited from 30 countries world over.

We expect Cipla should record revenue CAGR of 8.5% over FY18-20E, and report EBITDA margin of 18.67 and 19.54% in FY19E and FY20E led by domestic pharma market volume growth, global generic respiratory products opportunities, US market limited competition launches and outperformance by Cipla in African private market.

The company has significant revenue flowing in from respiratory products, which is a fast-growing segment and has less competition. Cipla has an excellent respiratory expertise and is ready to commercialize high margin inhalers opportunities in US and other regulated markets. We believe Cipla is well placed to capture the generic opportunities in inhalers space especially in the US market as novel inhalers space is still untapped because it is a difficult product to prove bioequivalence or conduct clinical trials. We expect Cipla to launch one Inhaler each year in the US starting from Albuterol in FY20 and Advair in FY21 and to file other ICS(Inhaled corticosteroids)/LABA(Long-acting beta agonists) products like Dulera, and Breo. We assume respiratory products story to be the dominant factor supporting our Buy recommendation.

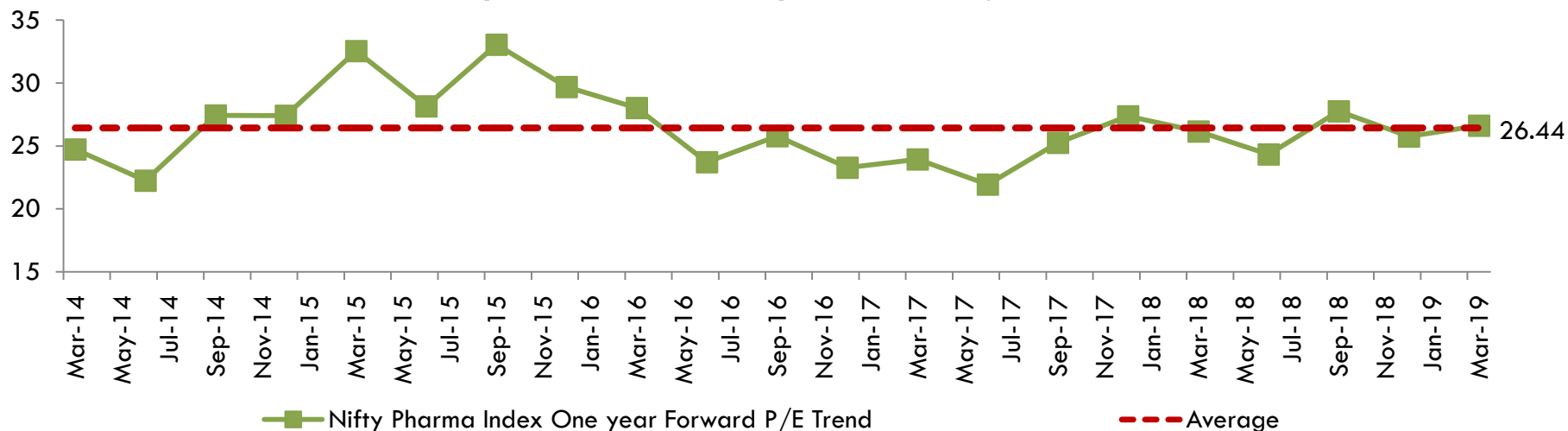
Companies transformation from a partnership business model to establishing a front-end presence in US and Africa will lead to an increase in Cipla's revenues and margins. We expect Cipla's US revenue to increase from current ₹2587Cr to ₹2898Cr in FY19 and ₹3477Cr in FY20 on account of new launches and an increase in DTM business.

We use a PE-based valuation approach for the pharmaceutical sector. **Cipla is currently trading at 30x FY19E P/E and 23x FY20E P/E.** At the current valuations, we see room for further re-rating for the company as we believe that opportunities in the inhalers space are immense. However, the valuation and our earnings estimate do not incorporate the risk of adverse outcome from the global pharma regulators for its facilities which can delay in monetization of respiratory product pipeline and key launches in the US and in other markets.

	EV/EBITDA		P/E		EV/SALES	
Security Name	FY 19 E	FY 20E	FY 19 E	FY 20E	FY 19 E	FY 20E
Cipla	15.81	13.05	29.77	23.41	2.85	2.59
Torrent Pharma	17.27	14.84	37.77	28.48	5.91	5.16
Alkem Lab	18.05	14.69	25.71	20.29	3.69	3.22
Ipca Labor	16.58	13.67	25.52	20.64	3.77	3.26

Source : Bloomberg Estimate

Nifty Pharma Index One year Forward P/E Trend



Source : Bloomberg

Domestic pharma companies valuation comparison with top global generic players

Indian Pharma companies trade at a premium valuation compared to leading global generic players, although Indian companies are less involved in developing innovative and complex products while global players have an edge over them in terms of experience and innovation. We believe the premium valuations are justified due to high gross margins and favorable capital structure of Indian companies. In the last few years, earnings of domestic pharma companies were temporarily muted because of several reasons like pricing pressure, regulatory hurdles, and INR stability. We believe pricing pressure will taper further in the US, INR depreciation will add benefits to pharmaceutical companies and regulatory issues will settle down further as companies start to become more compliant with the norms.

Major Global Generic Player in US

	Latest Gross Margin	Latest Net Debt/ EBITDA	One Year Forward P/E
Teva	44%	5.07x	6.44
Mylan	35%	3.70x	6.01

Major Indian Generic Player in US

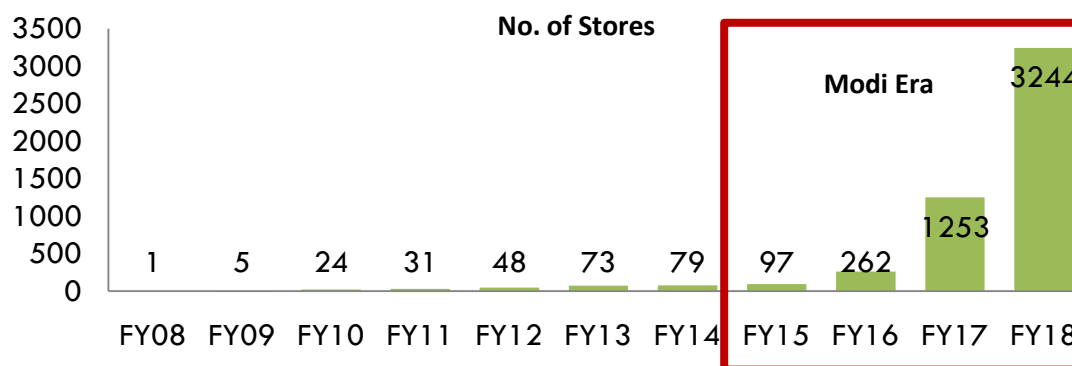
	Latest Gross Margin	Latest Net Debt/ EBITDA	One Year Forward P/E
Sunpharma	70%	-0.65x	27.46
DR.Reddy	71%	1.26x	25.42
Lupin	67%	1.75x	34.86

Source : Bloomberg

Investment Risk

Janausdhi program a possible threat to domestic market participant

Jan Aushadhi project was launched by Government of India in the year 2008 to provide quality medicines at affordable prices. The 'Jan Aushadhi Scheme' was revamped as 'PradhanMantri Jan Aushadhi Yojana' under Modi's leadership by making several changes to the scheme like increasing medicines under the scheme, widening therapeutic basket of drugs to offer, including private players to participate, increasing incentives and margins to start a store. With the tremendous increase in the numbers of new stores opened under Modi era and focus on providing medicines at affordable rates, this could lead to a risk for the branded generic players in the domestic pharmaceutical as the drugs available in Janausdhi are much cheaper than branded drugs.



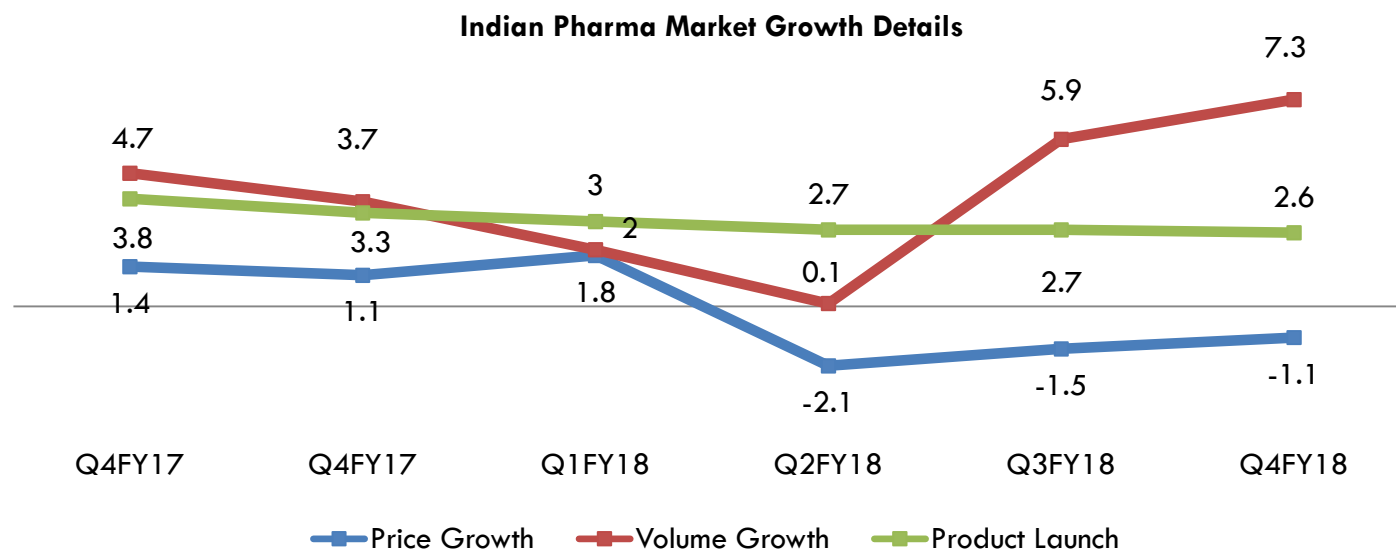
List of price difference between drugs available in Janushdhi Stores are branded drugs .

API	Dosage	Pack	Jan Aushadhi Price	Market Price
Tab. Ciprofloxacin	250 mg	10	14	55
Tab. Ciprofloxacin	500 mg	10	22	125
Tab. Diclofenac	100 mg	10	6.12	60
Tab. Cetrizine	10 mg	10	1.84	20
Tab Nimesulide	100 mg	10	2.7	40

Extending number of medicines under NLEM and FDC

India's drug pricing is controlled by the Department of Pharmaceuticals through the National List of Essential Medicines (NLEM). Prices of drugs under NLEM are capped by the government and the price revision takes place annually based on the wholesale price Index(WPI). With most of the drug market dominated by branded products, an extension of medicines under NLEM or any new measure by the Government to regulate the market will hurt the industry.

Recently, the Government has prohibited manufacturing and sale of 328 fixed-dose combinations (FDC) due to concern over patient safety. Prohibition nearly affected 6,000 brands from different therapies like painkillers, anti-diabetic, respiratory and gastrointestinal medicines and FDCs in India that form at least one-fourth of the total domestic pharma market. Companies like Pfizer, Procter & Gamble, Abbott, Glenmark, Sanofi, Wockhardt, Cipla, Lupin, Sun Pharma and Dr. Reddy may get affected as these companies contain Fixed Drug Combination in their product pipeline.



Government push towards the use of generic names for prescription

Prime Minister Narendra Modi has indicated a few times towards making a law which will require doctors to prescribe medicines by their generic/salt names with an aim to reduce health care expenses. With branded drugs making up to 90% of the Indian market, this move might have some destructive effect on the industry. If implemented retail pharmacists and distributors will have little incentive in stocking and selling low-priced generic medicines since they have lower profit margins as there is a huge cost difference between drugs amidst different brands.

Regulatory risk in the face of plant inspection

The Pharmaceutical industry is highly regulated by various regulators keeping a check on the quality of the manufacturing companies by regular inspection of their plants. Inspections of the manufacturing plants have been one of the key risk factors to the company's earnings growth due to disruption in existing revenue and delay in new product approvals as these inspection outcomes can be escalated to form 483, warning letter or import alert and the timeline for resolution has been also uncertain.

With increasing exposure in the US market every year and key product approvals pending, we expect inspection of various plants to take place in the form of GMP(Good Manufacturing Practices) or pre-approval Inspection. Although its track record so far has been clean, still there is a risk of disruption to the US business as the outcome by the regulator are unpredictable.

Delay in monetization of respiratory pipeline in the US market

We believe there could be a material risk to Cipla's US business if there is a delay in the launch of respiratory products. These products usually require clinical trials to prove bioequivalence and sometimes additional data after receiving CRLs from the regulator. For instance, leading pharma companies Mylan and Teva have received CRLs for Advair. Delay in approvals of inhalers for Cipla might lead to difficulty in capturing the market and its earnings realization.

Margin erosion from Invagen's product portfolio

We expect products launched from Invagen to face pricing pressure due to the nature of the product and increase in competition in the US. Therefore by raising concerns for Invagen products pipeline could possibly create haul on companies margin performance, as the margin of Invagen is comparatively lower than Cipla's own front end and B2B business.

Currency risk

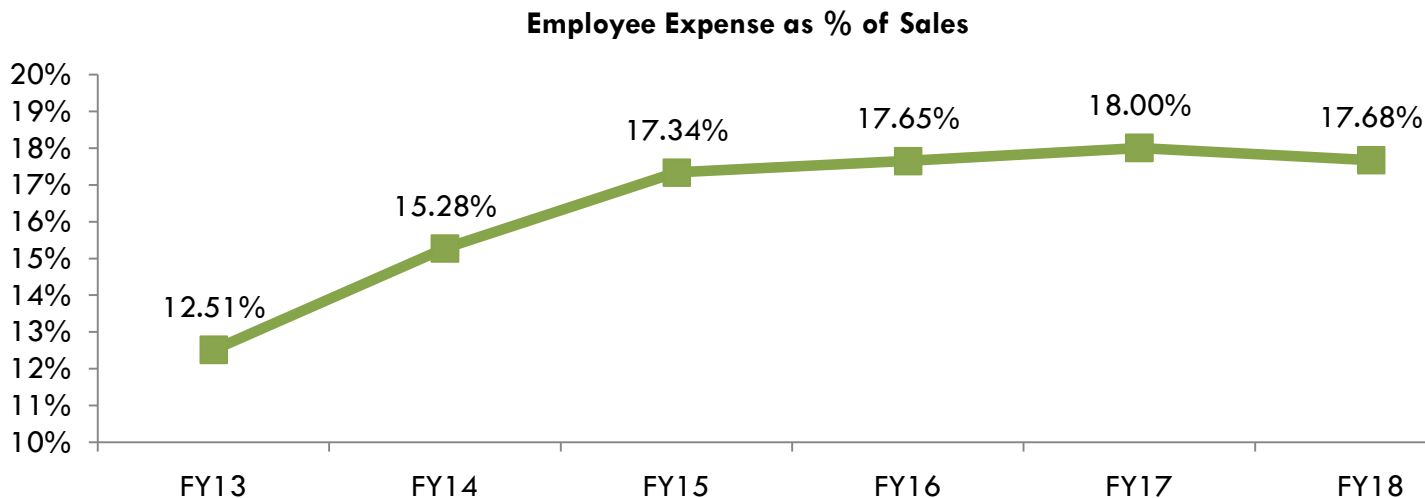
Cipla earns the highest revenues among Indian peers from emerging markets economies. Cipla generates nearly 22% of consolidated revenue from emerging markets with exposure to countries like Australia, Africa, Myanmar, and Nepal. Emerging markets currencies are very volatile in nature which can dampen the revenues and profit in rupee terms.

Escalating API prices

The prices of APIs from China have gone up tremendously in the last few months because of the crackdown by the local government on industries allegedly polluting the environment. China is the biggest supplier of APIs to Indian pharma companies, accounting for almost 60 % of the total imports of the ingredients. With pricing pressure in the US market still visible, formulation players could face a tough time if they are unable to pass on the higher raw materials price to the end users.

Frequent management change and high employee expense cause of concern

In last few years, Cipla has turned itself from a family managed company to a professionally managed one, which has lead to hiring many professionals across various regions and departments. In 2013 after Dr. Y K Hamied stepped down as MD, Cipla appointed Subhanu Saxena as the company's CEO & he focused on building front-end operation in the US and Europe. Under Subhanu's leadership, Cipla acquired Invagen and Exelan in 2015, picked up a stake in Chase Pharma and acquired Medpro. During Subhanu's tenure, we witnessed a stream of acquisitions and a significant increase in the employee expenses which lead Cipla's underperformance compared to its peers. In 2016, Subhanu was replaced by Umang Vohra as the global CEO and he took on the task to restructure the company by exiting several non-core operations and focusing on profitability. We believe a frequent change in management level can delay in achieving the milestone and escalate employee cost.



Source : Company Reports

Financials

Income Statement

(₹ Cr)

	FY16	FY17	FY 18	FY19E	FY 20E
Total Revenue from Operation	13,790	14,630	15,219	16,337	17,973
Other Income	208	229	358	358	358
Total Income	13,998	14,859	15,577	16,694	18,331
Raw Material	5,090	5,317	5,438	6,045	6,470
Employee Benefit Expense	2434	2634	2690	2892	3235
Finance Costs	207	159	114	85	80
Depreciation & Amortization Expense	754	1,323	1,323	1,026	831
Other Expense	3,787	4,204	4,264	4,623	5,032
Total Expense	12,271	13,637	13,830	14,671	15,648
Profit Before Tax	1,727	1,222	1,747	2,023	2,682
Tax Expense	332	180	250	567	751
Net Profit	1395	1042	1497	1457	1931
EPS	17.17	12.51	17.51	18.08	23.96
EPS Growth YoY in %	17.1%	-27.1%	39.9%	3.2%	32.6%
EBITDA	2481.25	2476	2831	3050	3513
EBITDA Growth YoY in %	14.77%	-0.21%	14.33%	7.74%	15.18%

Balance Sheet

(₹ Cr)

Balance Sheet	FY16	FY17	FY 18	FY19E	FY 20E
Assets					
Non Current Assets					
Net Property , Plants & Equipment	4,605	5,009	5,315	5,389	5,558
Capital Work in Progress	741	719	512	512	512
Good Will	2,706	2,697	2,815	2,815	2,815
Intan Asset + Under Dev+ Inv in Assoc	3,396	2,763	2,299	2,299	2,299
Financial Assets					
Investments & Loans	200	163	189	189	189
Other Financial Asset	561	714	729	729	729
Deferred Tax Assets (Net)	79	168	188	188	188
Total Non Current Assets	12,287	12,232	12,046	12,120	12,289
Current Assets					
Inventories	3,808	3,485	4,045	4,471	4,839
Financial Assets					
Investments	582	837	1102	1102	1102
Trade Receivables	2,356	2,563	3,102	3,223	3,693
Cash and Cash Equivalents	858	610	853	774	1,232
Other than Cash and Cash Equivalents	13	14	112	112	112
Loans & Other Current Asset	1223.17	1225.64	1599.13	1599.13	1599.13
Total Current Asset	8,841	8,736	10,814	11,282	12,578
Total Asset	21,128	20,968	22,861	23,402	24,867

Balance Sheet (Contd)

(₹ Cr)

Balance Sheet	FY16	FY17	FY18	FY19E	FY20E
Equity & Liabilities					
Equity					
Equity Share capital	161	161	161	161	161
Other Equity	11,356	12,383	14,068	15,370	17,147
Equity attributable to owner	11,516	12,544	14,229	15,531	17,308
Non Controlling Interest	350	438	352	352	352
Total Equity	11,866	12,982	14,582	15,884	17,660
Non Current Liabilities					
Financial Liabilities					
Borrowings	222	3,645	3,662	3,400	3,200
Provisions	145	141	138	138	138
Deferred Tax Liabilities(Net)	976	757	503	503	503
Other Financial Liabilities	42	45	50	50	50
Other Non Current Liabilities	101	94	93	93	93
Total Non Current Liabilities	1,486	4,681	4,447	4,185	3,985
Current Liabilities					
Financial Liabilities					
Borrowings	4,970	467	436	400	350
Trade Payables	1,476	1,571	2,119	1,656	1,595
Other Financial Liabilities	738	574	420	420	420
Other Current Liabilities	593	693	857	857	857
Total Current Liabilities	7,776	3,305	3,832	3,333	3,223
TOTAL EQUITY AND LIABILITIES	21,128	20,968	22,861	23,402	24,867

(₹ Cr)

Cash Flow Statement	FY16	FY17	FY 18	FY19E	FY 20E
CASH FLOW FROM OPERATING ACTIVITIES					
Net profit before tax	1,727	1,222	1,670	2,023	2,682
Depreciation and amortisation expense	754	1,323	1,323	1,026	831
Other Adjustment	197	51	-25	111	106
Change in Working Capital	-429	235	-783	-1,010	-899
Tax Paid	-508	-450	-722	-567	-751
Net cash flow generated from operating activities	1,741	2,382	1,463	1,585	1,968
CASH FLOW USED IN INVESTING ACTIVITIES					
Net Purchase of PPE & CWIP	-1,077	-1,136	-816	-1,100	-1,000
Other Adjustment	-3446	-174	-38	0	0
Net cash flow used in investing activities	-4,523	-1,310	-854	-1,100	-1,000
CASH FLOW FROM FINANCING ACTIVITIES					
Issuance of equity share capital & Transaction with Non Contr Int	3	108	-44	0	0
Proceeds/Repayment of borrowings	3442	-1082	-34	-298	-250
Interest paid	-161	-159	-118	-85	-80
Dividends paid on equity shares	-159	-159	-161	-161	-161
Tax paid on equity dividend	-20	-33	-28	-20	-20
Net cash flow generated from/(used in) financing activities	3104	-1326	-385	-564	-511
Net increase/(decrease) in cash and cash equivalents	323	-254	224	-79	458
Cash and cash equivalents at the beginning of the year	546	858	610	854	775
Exchange difference on translation	-10	6	20	0	0
Cash and cash equivalents at the end of the year (refer note 15)	858	610	854	775	1,232

Ratios	FY16	FY17	FY 18	FY19E	FY 20E
Gross Margin	63.09%	63.66%	64.27%	63.00%	64.00%
EBITDA Margin	17.99%	16.92%	18.60%	18.67%	19.54%
RoE (%)	10.03%	7.07%	9.31%	8.92%	10.75%
Net Debt / Equity	0.31	0.20	0.14	0.11	0.06
Net Debt/ EBITDA	1.51	1.07	0.72	0.59	0.31

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Name of the Security	Cipla Ltd.
Name of the analyst	Tausif Shaikh
Analysts' ownership of any stock related to the information contained	NIL
Financial Interest	
Analyst :	No
Analyst's Relative : Yes / No	No
Analyst's Associate/Firm : Yes/No	No
Conflict of Interest	No
Receipt of Compensation	No
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