

Lupin

Rs1782
OUTPERFORMER

RESULT NOTE

Mkt Cap: Rs160bn; US\$3.5bn

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Result : Q4FY10

Comment : In line; Lotrel to boost near term growth

Last report : 29 January 2010 (Price Rs1420; Recommendation: Outperformer)

Key valuation metrics

As on 31 March	Net sales (Rs m)	Adj. net profit (Rs m)	Adj. EPS (Rs)	% change	PE (x)
FY08	27,063	4,083	45.4	30	39.3
FY09	38,472	5,791	64.3	42	27.7
FY10E	48,708	6,997	77.7	21	22.9
FY11E	57,307	8,474	94.2	21	18.9
FY12E	65,161	9,993	111.0	18	16.0

Highlights of Q4FY10 and FY10 results

- ♦ Lupin's net profits for Q4FY10 grew by 40%yoy to Rs2.2bn (we saw at Rs2.1bn). Lower effective tax rate (at 11.5%) and higher other operating income (at Rs538m) saw net profits marginally ahead of our estimates. EBITDA for the quarter stood came at Rs2.5bn (we saw at Rs2.6bn) with operating margins expanding by 127bps yoy to 19.4% (we saw at 19.7%). Net sales grew by 23%yoy to Rs12.8bn. R&D Expenses for the quarter stood at Rs1.1bn, 8.8% of sales.
- ♦ Lupin has recommended dividend of 135% on each share of face value of Rs10/- and has announced a stock split of 1:5.
- ♦ For the full year, Lupin' net sales and profitability grew by 26% and 36%yoy to Rs47.4bn and Rs6.8bn respectively. EBITDA stood at Rs8.5bn with operating margins of 20.2%
- ♦ Lupin in Q4FY10 filed 28 ANDA's as against 9ANDA's over 9MFY10. Lumped filing in Q4FY10 in our view could be a key reason for surge in R&D costs for the quarter. R&D costs (as % of sales) for the quarter stood at 8.8%.
- ♦ Interest costs declined by 28%qoq to Rs78m. Management attributed working capital release along with lower borrowing costs to be the key reasons for decline. Working capital has declined to 91 days from 110 days in the previous year
- ♦ Lupin's R&D expenditure for the year stood at Rs3.5bn translating to 7.5% of sales for FY10. Lupin is today amongst the most prolific R&D spenders in the industry which we believe bodes well for future growth.
- ♦ Lupin's net debt stands at Rs9.4bn at end-Q4FY10 with a debt-equity ratio of 0.35x.
- ♦ Lupin incurred a capex of Rs4.4bn in FY10 and plans to incur a capex of ~Rs5.5bn in FY11
- ♦ ROCE has expanded to 25%.

□ US – Lupin’s Crown Jewel

- ♦ US sales grew by 39%yoy to Rs16.5bn for FY10 with growth in branded portfolio including Antara, Suprax and Aerochambers. Branded business grew by 72%yoy (at US\$127m) and contributed 37% to US formulation sales. Lupin is expecting to launch 6 new products in FY11 and is looking to launch 80+products over next 3years (v/s 25 products in last 4years).
- ♦ Lupin maintained its numero uno position of the fastest growing generic company in the US market for second consecutive year. 12 of its 25 product launches enjoy no. 1 position based on market share. 22 of the 25 product launches feature amongst top 3 products by market share.
- ♦ Lupin launched generic Lotrel in February 2010 after reaching a settlement with Novartis and has attained a marketshare of 26%, much higher than our estimates of 10-15%. With product market currently hovering around ~\$400mn and incremental competition not very likely in FY11, Lotrel is set to be a huge product for Lupin in FY11 and FY12. We estimated Lupin to generate atleast \$65-70mn sales in FY11 on the product with extremely healthy margins.
- ♦ Lupin expects approvals launch of oral contraceptives (OC) products in US from FY12 onwards. Lupin has filed around 22 ANDAs on OCs and will enter the market with a whole suite of products which will significantly enhance its competitiveness. Lupin remains upbeat on its superior OC product offering (v/s domestic peers) and indicated given its vertical integration, the company would have an edge over other global majors like Teva, Mylan and Watson. Lupin looks to get approval for 6-8 critical products in the space before commercializing its ANDAs.
- ♦ Lupin has filed 127 ANDA’s till now of which 41 ANDA’s have secured approval. Lupin in Q4FY10 filed 28 ANDA’s as against 9ANDA’s over 9MFY10. Management indicated 34 of its ANDA filings had Para IV status and 11 FTF. Lupin expects to have full exclusivity on Glumetza, Fortamet and Cipro DS amongst 11 FTF. Lupin targets 30-40% of its incremental ANDA filing to be P IV. Post OCs, Ophthalmology is another ticket target segment for Lupin. The company is looking to target a new therapeutic area each year.
- ♦ Lupin remains fairly positive on the potential for Antara to reach ~\$70-80mn by FY11. On the branded side, Lupin has increased its field force in US from 70 to 170 by end 4QFY10 to promote Antara. The increased field force will also be used to promote Allernase which is expected to be launched by Q2FY11. Lupin indicated Antara sales were largely flat over last 4months and ramp-up in field force and marketing efforts had successfully restricted the decline in sales. Lupin remains positive on its ability to protect the profitability of its branded product franchise despite the sharp addition of field force over the next few quarters.
- ♦ On Suprax, Lupin believes that near term competition is not imminent which is likely to protect the Suprax franchise through FY11. Further Lupin believes that even generic competition entry is unlikely to completely erode the sales across the entire franchise as the line extensions are unlikely to be impacted. Lupin is also looking a couple of line extensions which may potentially switch the entire franchise to these new variants. Conservatively, factoring in a likely Suprax generics entry by FY12, we have assumed \$50mn Suprax sales in FY12 down from \$90mn in FY11.

□ Other Markets

- ♦ Lupin’s Japanese subsidiary, Kyowa, has reported a constant currency growth of ~21% yoy (to Rs5.3bn) contributing 11% to overall revenues. Lupin remains bullish on the generic opportunity in the Japanese market. Kyowa launched 4 new products – levofloxacin, saypogreate, rebamipide and bicalutamide during the year. Kyowa currently undertakes its marketing operations via 70 strong field force catering to CNS, CVS and GI segments. Kyowa’s operating margin expanded by 300bps yoy to 41% for the quarter. This improvement in margins was without any contribution from Lupin. The Japanese markets are currently being serviced by the Osaka unit. Management indicated the margins would see further expansion once production from Osaka unit is shifted to India. Management has indicated that the process of securing regulatory approvals for its Indian facility is progressing well though it is still a year away.
- ♦ In the domestic market, Lupin remains one the fastest growing companies with growth of 28%yoy to Rs13bn. Superior growth was primarily on back of strong performance and rising market share in the CVS, Diabetes, CNS, Asthma and Gastro therapy Segments. Lupin plans to enter Oncology segment in foreseeable future. Lupin launched 42new products in FY10. 10 of Lupin’s brands enjoyed sales over Rs250m, whereas 13 and 9 brands saw sales in the

range of Rs150-250m and Rs100-150m respectively. Lupin currently has 3682 strong field force and plans to steadily ramp-up going forward accompanied with new product launches.

- ♦ Lupin's South African acquisition, Pharmadynamics, has also grown strongly at 57%. Lupin enjoys leadership position in CVS segment and is ranked amongst 6th largest generic companies in South Africa.

Valuation & view

Lupin's revenues and net profits for Q4FY10 grew by 23% and 40%yoy. Lupin remains amongst the most prolific R&D spenders in the industry which we believe bodes well for its future growth. With critical mass across the key generic markets of US, Japan and India (backed by very quality product pipeline) and remarkable success in branded business in US, Lupin is clearly one of the most scalable model in the Indian pharma industry. Lupin remains one of our top picks in the space with exciting upside possibilities as its high quality ANDA pipeline (142 filings, including 34 Para IV and 11 first to files) in US begins to unfold with the launch of oral contraceptives, ophthalmic, controlled release products, FTFs as well as niche products. We believe this will enable Lupin to effectively neutralize the impact of any likely Suprax generics entry. **We upgrade Lupin's FY11 and FY12 earnings by 5.2% and 4.1% respectively primarily due to higher contribution expected from Lotrel.** Given Lupin's superb growth performance over last several quarters, exciting growth outlook, significant scale (FY12e PAT – Rs10bn), strong balance sheet (25% ROCE) and possibilities for upsides, we believe the stock now deserves to trade in line with large cap peers and should get further re-rated. Reiterate Outperformer with a 15 month price target of Rs2220 (20x FY12E and 23.6x FY11E). Lupin is our top pick in the space.

Quarterly results

Particulars (Rs m)	Q4FY09	FY09	Q1FY10	Q2FY10	Q3FY10	Q4FY10	Particulars
Net Sales	10,434	38,472	10,856	11,147	12,554	12,848	Net sales marginally below our estimates
Operating Expenses	8,544	33,178	8,914	9,506	10,090	10,358	
Cost of Sales	4,910	16,043	4,676	5,013	5,122	4,882	
Other Expenses	3,634	17,135	4,238	4,493	4,968	5,475	
EBITDA	1,890	7,520	1,942	1,641	2,464	2,491	
EBITDA	18.10	19.50	17.90	14.70	19.60	19.40	OPM were marginally below our estimates
Other Income	258	954	211	541	155	539	
Depreciation	266	880	231	242	358	408	
Interest	124	499	107	91	109	78	
PBT	1,758	7,096	1,815	1,848	2,152	2,543	
Extraordinary		(322)					
Provision for Taxation	139	983	364	200	504	293	
Tax rate	0		0	0	0	0	
Minority and share in associate loss (44)			(50)	(43)	(42)	(45)	
PAT	1,574	5,791	1,401	1,604	1,606	2,206	Lower effective tax rate (at 11.5%) and higher other operating income (at Rs538m) saw net profits marginally ahead of our estimates.
yoy growth (%)							
Net Sales	39.0	42.2	25.9	22.7	30.5	23.1	
EBITDA	57.9	72.6	27.2	(10.0)	60.3	31.8	
Net Profit	63.7	41.8	25.1	38.7	37.0	40.2	

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