

BSE Sensex 19,640	S&P CNX 5,959
Bloomberg	CIPLA IN
Equity Shares (m)	802.9
M.Cap. (INR b)/(USD b)	325.2/6.1
52-Week Range (INR)	435/287
1,6,12 Rel. Perf. (%)	-4/4/4

Financials & Valuation (INR b)

Y/E March	2013E	2014E	2015E
Sales	83.0	89.7	102.6
EBITDA	22.0	22.4	25.6
Net Profit	13.5	15.8	18.2
Adj. EPS (INR)	16.8	19.7	22.6
EPS Gr. (%)	20.2	16.8	14.9
BV/Sh. (INR)	110.5	125.2	142.2
RoE (%)	15.2	15.7	15.9
RoCE (%)	22.6	20.7	21.4
Payout (%)	20.0	25.0	25.0
Valuations			
P/E (x)	24.0	20.6	17.9
P/BV (x)	3.7	3.2	2.8
EV/EBITDA (x)	14.8	14.5	12.7
Div. Yield (%)	0.8	1.0	1.2

CMP: INR405
TP: INR452
Neutral

- Revenues grew 18% YoY to INR20.71b (v/s est INR20.17b), EBITDA grew 26% YoY to INR4.93b (v/s est INR4.71b) and PAT was up 26% to INR3.39b (v/s est INR3.25b). Top line growth was primarily led by 38% YoY growth in export formulations, while domestic formulations grew a modest 10% YoY. Export APIs stood at INR1.38b and declined by 16% YoY on a high base.
- We are positively surprised by the strong growth in export formulations, driven by Lexapro supplies (now part of the base business) and strong growth witnessed across key therapeutic areas. Also, there was a 6-7% benefit from currency; however, management indicated that this high growth is not sustainable, going forward. The muted domestic formulations growth of 10% is below our expectation of 15%.
- EBITDA margin increased 150bp YoY and stood at 23.8% (v/s our est of 23.3%). Margin improvement was driven by favorable product mix, with higher contribution from anti-depressants segment (includes generic Lexapro supplies, now part of base business) and anti-allergics (includes Dymista, currently a small contributor).
- PAT growth was aided by strong top line growth coupled with healthy operational performance. There was a forex gain of INR190m for the quarter.

While export formulations grew 38% YoY in 3QFY13, Cipla's core quarterly performance has not been encouraging in the past many quarters. Its muted export performance had raised uncertainty on the timelines of ramp-up at Indore SEZ. We believe it is imperative for the company to improve asset utilization at Indore to drive future growth and derive benefits of operating leverage (overhead expenses continue to adversely impact performance). Post 3QFY13 performance, our core EPS est for FY13E has witnessed an upgrade of 2%, while FY14E/15E est are largely unchanged. Our revised est take into account better-than-expected performance in export formulations during this quarter, partially offset by the muted growth in domestic formulations. The stock trades at 20.6x FY14E and 17.9x FY15E EPS. Maintain **Neutral** with a TP of INR452 (20x FY15E EPS).

Quarterly Performance

Y/E March	FY12				FY13				FY12	FY13E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Net Revenues	15,914	17,780	17,580	18,530	19,582	21,881	20,705	20,823	70,207	82,991
YoY Change (%)	7.5	10.1	13.2	11.2	23.0	23.1	17.8	12.4	11.2	18.2
Total Expenditure	12,219	13,404	13,666	14,330	14,183	15,149	15,776	15,923	53,619	61,032
EBITDA	3,695	4,376	3,915	4,200	5,399	6,732	4,929	4,900	16,589	21,959
Margins (%)	23.2	24.6	22.3	22.7	27.6	30.8	23.8	23.5	23.6	26.5
Depreciation	703	656	757	1,006	728	740	780	877	3,122	3,125
Interest	43	24	32	22	11	54	93	17	383	175
Other Income	249	243	302	390	531	641	535	9	1,395	1,716
Profit before Tax	3,199	3,939	3,426	3,561	5,190	6,580	4,591	4,015	14,478	20,376
Tax	666	850	727	794	1,182	1,618	1,203	887	3,036	4,890
Rate (%)	20.8	21.6	21.2	22.3	22.8	24.6	26.2	22.1	21.0	24.0
Reported PAT	2,533	3,090	2,699	2,767	4,008	4,963	3,388	3,127	11,442	15,485
Adj PAT	2,533	3,090	2,699	2,577	3,057	3,949	3,388	3,127	11,252	13,521
YoY Change (%)	-1.6	17.5	16.0	20.3	20.7	27.8	25.5	21.3	16.3	20.2
Margins (%)	15.9	17.4	15.4	13.9	15.6	18.0	16.4	15.0	16.0	16.3

E: MOSL Estimates

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3QFY13 top line was in line with estimates

Cipla's revenues grew 17.8% YoY to INR20.7b (v/s estimate of INR20.17b), core EBITDA grew 26% YoY to INR4.93b (v/s estimate INR4.71b) and PAT grew 25.5% to INR3.39b (v/s estimate INR3.25b).

Top line growth was primarily led by 38% YoY growth in export formulations but tempered down by a 10% growth in domestic formulations. API exports reported a 16% decline YoY to INR1.38b on account of a high base.

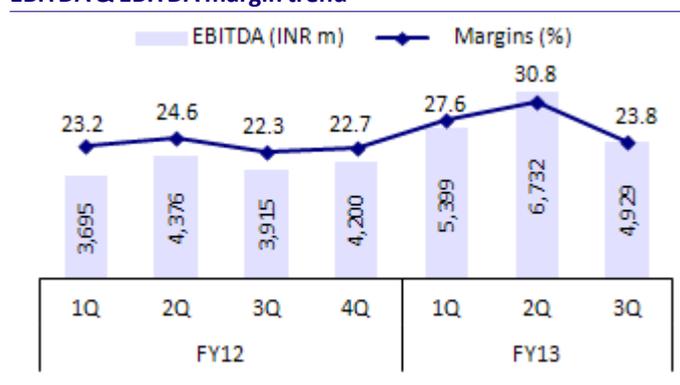
We are positively surprised by the strong growth in export formulations, driven by Lexapro supplies (now part of the base business) and the strong growth witnessed across key therapeutic areas. Also, there was a 6-7% benefit from currency; however, management indicated that this high growth is not sustainable, going forward. The muted domestic formulations growth of 10% is below our expectation of 15%.

Sales mix (INR m)

	3Q FY13	3Q FY12	YoY (%)	2Q FY13	QoQ (%)
Domestic	9,240	8,457	9.3	9,294	(0.6)
% of revenues	45	48		42	
Exports	11,067	8,658	27.8	12,127	(8.7)
% of revenues	53	49		55	
Formulations	9,692	7,022	38.0	10,389	(6.7)
APIs	1,375	1,637	(16.0)	1,738	(20.9)
Other Oper. Income	398	465	(14.5)	460	(13.4)
% of revenues	2	3		2	
Total Net Revenues	20,705	17,580	17.8	21,881	-5.4

Source: Company, MOSL

EBITDA & EBITDA margin trend



Source: Company, MOSL

EBITDA above estimate aided by favorable product mix

EBITDA grew 26% YoY to INR4.93b (v/s est of 20.3% to INR4.71b). EBITDA margin increased 150bp YoY and stood at 23.8% (v/s our est of 23.3%). This margin improvement was driven by favorable product mix, with higher contribution from anti-depressants segment (includes generic Lexapro supplies, now part of base business) and anti-allergics (includes Dymista, currently a small contributor).

We believe the EBITDA contribution from generic Lexapro supplies, compared to 2QFY13, has reduced more than the reduction in its revenue contribution. This could be attributed to the pressure on Teva's profitability after the 180-day exclusivity and increased generic penetration in the escitalopram market.

PAT growth was aided by strong top line growth coupled with healthy operational performance. There was a forex gain of INR190m for the quarter.

Management retains guidance for FY13

- While the management did not specifically discuss the overall top line growth guidance for FY13, it had earlier guided for 15% growth. Domestic formulations are guided to grow by more than 15% YoY for the year and the management is confident of sustaining this momentum in FY14.
- EBITDA margin is expected to improve on account of better product mix and positive impact of favorable currency. Management indicated that EBITDA margin at 22-23% can be expected, going forward.
- Tax rate guidance has been maintained for FY13/14 at 23-24%. Capex guidance has been retained at INR5b for FY13, with INR3-4b guided for FY14. Forex hedges are at USD210m.

FY13 Guidance

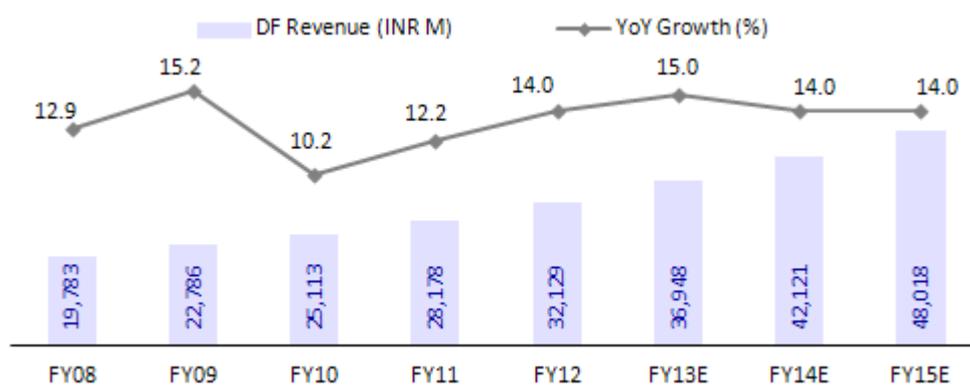
Business	Revised guidance	Remarks
Overall top line growth (%)	Over 15%	To be driven by 15%+ growth in domestic formulations. Growth in export formulations to moderate, going forward
EBITDA margin (%)	Improved margins	We estimate core EBITDA margin of 24-25%
Capex (INR b)	5.0	Capex mainly directed towards API & R&D capacity expansion

Source: Company, MOSL

Domestic formulations record healthy 17% growth in 9MFY13 - unlikely to sustain in coming quarters

- Cipla is a dominant player in domestic formulations (DF) market, enjoying No. 2 ranking in the industry, supported by a field force of ~7,500 MRs. This business contributes ~45-50% of its overall revenues and is a key earnings driver.
- Company had reported 14% YoY growth in this business in FY12, post muted performance in FY10 and FY11. After reporting a strong growth of 22% for 1HFY13, the business recorded a muted 10% growth this quarter.
- The strong growth recorded in 1HFY13 is unlikely to recur, also confirmed by the management. Company has guided for 15%+ YoY growth for this business for FY13 and expects to maintain 14-15% growth in FY14. We have cut our growth estimate to 15% for this business for FY13E (down from 18%) and have retained 14% growth for FY14E/15E.
- Management did not indicate the potential impact of the drug pricing policy on its domestic business and will await the formal implementation of the policy before sharing details.

Cipla - Domestic Formulations (DF) - Revenue Ramp-up

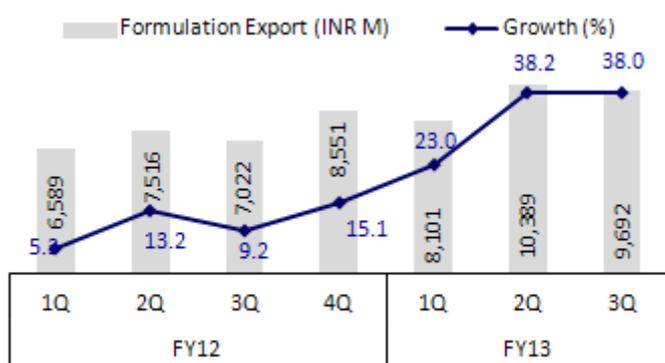


Source: Company, MOSL

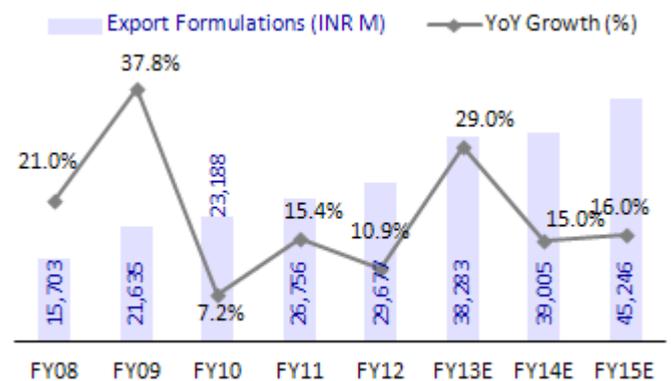
Core export formulations to show moderate growth in future

- Despite the strong 38% YoY growth in 3QFY13, Cipla's core quarterly performance in export formulations has not been encouraging in the past many quarters. This was particularly disappointing given favorable currency (Cipla does not have very high hedges). Management also indicated that the high growth reported in this quarter will not sustain, going forward.
- There are ~76 approvals for ANDA filed along with its partners, of which 60% have been commercialized. While there are another 23 ANDAs under the registration process, we believe their commercialization will take another 2-3 years.
- Management indicated that it continues with the product-cum-geographical rationalization of this business to ensure focus only on profitable products/geographies. While profitable rationalization is a long term positive, we are cautious on this business and have factored a moderate growth rate of 15%/16% for FY14E/15E. We note the strong growth so far in FY13 has mainly been driven by one-off supplies of generic Lexapro.

Cipla's Export Formulation - Muted Quarterly Performance...



...Moderate growth expected ahead



Note-4QFY12 & 1HFY13 includes one-time supplies of generic Lexapro

Source: Company, MOSL

Indore SEZ approved by US FDA - A step towards building own front-end in US

- Management is planning direct entry into the US market; till date it accessed the US market through partnerships.
- We believe that Cipla will be a very late entrant in the US and hence may not be able to generate adequate returns. The recent approval (received in 2QFY13) of the Indore SEZ by the US FDA will facilitate Cipla's entry in the US as it plans to file ANDAs from this facility in its own name, compared to the previous practice of filing through partners.
- Company has already filed 5 ANDAs till date.

Dymista opportunity - Will take time to scale up

- Cipla's Swedish partner, Meda, had received final US FDA approval for Dymista in May-12. Dymista is a nasal spray and consists of a combination of Azelastine HCl and Fluticasone Propionate and is useful in treating seasonal allergic rhinitis. It reduces the quantum of allergy medicines that a patient needs to consume and offers better efficacy compared to traditional first-line treatments. The US patent office has issued two patents for Dymista expiring in 2023 and 2026.

- Cipla is a development-cum-manufacturing partner for Meda for Dymista. The partnership covers many markets, including the US. Cipla recently started supplies to support the US sales and Meda is expected to launch the product in the European market within the next two quarters.
- A few reports indicate that Dymista can generate annual revenues of USD350m in the US by 2016 for Meda. Cipla is likely to benefit as it will be supplying the global requirements for Dymista, including that for the US. While this may not entail any significant upside in the near term for Cipla (management has guided it expects it to be a USD25-30m revenue opportunity over the next few years), we view it as a long term positive for Cipla.

Cipla Medpro South Africa (CMSA) acquisition - to provide front-end in South Africa

- Cipla had earlier proposed to acquire Cipla Medpro South Africa (CMSA) for USD220m, valuing Cipla-Medpro at 7.7x and 6.8x EV/EBITDA for CY12 and CY13 respectively based on Bloomberg consensus estimates for CMSA. For CY11, it had reported revenues of USD244m, EBITDA of USD74m (EBITDA margins of 30.4%) and PAT of USD50m.
- This proposed acquisition will require various government and other approvals.
- CMSA is one of South Africa's top 10 pharmaceutical groups. The group's operations comprise of two divisions: 1) selling chronic and OTC medicines to the public and private sector and 2) contract manufacturing services.
- In Nov-12, and post Cipla (India)'s proposal, Cipla Medpro won a contract from the African Government to supply AIDS drugs. This delayed the acquisition as both the parties are now reconsidering the originally proposed terms of the acquisition. We await further clarity from the management on the way forward.
- We do not expect significant upside from this acquisition in the near term. CMSA has intangibles of USD170-180m which account for almost 50% of its total assets and will reflect on Cipla's balance sheet.

Cipla Medpro - Key Financials

(INR M)	CY11	CY12E	CY13E	CY14E
INR/USD	48	54.5	53	53
Sales	11,747	13,467	15,329	16,835
YoY Growth (%)		14.6	13.8	9.8
EBITDA	3,565	3,206	3,656	4,033
EBITDA Margins (%)	30.4	23.8	23.8	24.0
PAT	2,400	1,936	2,318	2,652
YoY Growth (%)		-19.3	19.7	14.4
ROCE (%)	19.7	17.8		
RoE (%)	15.1	14.6	15.4	15.8

Source: Bloomberg

Valuation and view

While export formulations grew 38% YoY in 3QFY13, Cipla's core quarterly performance has not been encouraging in the past many quarters. Its muted export performance had raised uncertainty on the timelines of ramp-up at Indore SEZ. While this facility recently got approved by the USFDA, Cipla expects to generate sales of INR6b from this facility in FY13 (same as in FY12). Although the large capex (for past few years) is a long term positive, we believe it is imperative for the company to improve asset utilization at Indore to drive future growth and derive benefits of operating leverage (overhead expenses continue to adversely impact performance).

Post 3QFY13 performance, our core EPS estimates for FY13E has witnessed an upgrade of 2% while FY14E/15E estimates are largely unchanged. Our revised estimates take into account better-than-expected performance in export formulations during this quarter, but the muted growth in domestic formulations has offset this upside. We estimate core EPS of INR19.7 for FY14E (up 17% YoY) and INR22.6 for FY15E (up 16% YoY). Based on our revised estimates, the stock trades at 20.6x FY14E and 17.9x FY15E earnings. We maintain **Neutral** with a target price of INR452 (20x FY15E EPS), 12% upside.

Cipla: an investment profile

Company description

Cipla is the largest player in the domestic formulations market and has a presence across most therapeutic areas. Company also has robust exports to several markets, including the US, Europe, South Africa, Australia and the Middle East. Cipla's strategy for regulated markets (Europe and the US) exports is built around supply tie-ups with global players.

Key investment arguments

- Strong capex of past years yet to be fully utilized - a long term positive.
- Commencement of exports of CFC-free inhalers to Europe will be a key positive; Cipla has the third largest capacity of inhalers in the world and could be a key beneficiary of the unfolding opportunity in the long term.

Key investment risks

- NPPA liability of INR16b (if it materializes) could result in a significant one-time cash outflow.
- The new pharmaceutical policy (proposed) has raised uncertainties regarding pricing of drugs in India. Further clarity on this is awaited.
- Cipla is planning to establish front-ends in some of the key markets - this could involve upfront investments and long gestation.

Comparative valuations

		Cipla	DRL	Ranbaxy
P/E (x)	FY14E	20.6	17.1	16.9
	FY15E	17.9	15.7	13.8
P/BV (x)	FY14E	3.2	4.0	2.7
	FY15E	2.8	3.7	2.3
EV/Sales (x)	FY14E	3.6	2.9	1.9
	FY15E	3.2	2.9	1.7
EV/EBITDA (x)	FY14E	14.5	14.1	13.7
	FY15E	12.7	12.2	11.5

Shareholding pattern (%)

	Dec-12	Sep-12	Dec-11
Promoter	36.8	36.8	36.8
Domestic Inst	11.8	13.4	20.4
Foreign	26.2	24.4	16.5
Others	25.2	25.4	26.3

Recent developments

- Proposes to acquire 51% stake in Cipla Medpro South Africa.
- Cipla Medpro wins AIDS drug contract from the African Government.

Sector view

- Differentiated portfolio in the US and emerging markets would remain the key sales and profit drivers in the medium term. Japan is expected to emerge as the next growth driver, particularly for companies with a direct marketing presence.
- We are overweight on companies that are towards the end of the investment phase, with benefits expected to start coming from the next fiscal.

Valuation and view

- While export formulations grew 38% YoY in 3QFY13, Cipla's core quarterly performance has not been encouraging in the past many quarters.
- Its muted export performance raises uncertainty on the timelines of ramp-up at Indore SEZ
- Based on our revised estimates, the stock trades at 20.6x FY14E and 17.9x FY15E earnings. We maintain **Neutral** with a target price of INR452 (20x FY15E EPS).

EPS: MOSL forecast v/s consensus (INR)

	MOSL Forecast	Consensus Forecast	Variation (%)
FY13	16.8	19.2	-12.3
FY14	19.7	20.7	-4.7

Target Price and Recommendation

Current Price (INR)	Target Price (INR)	Upside (%)	Reco.
405	452	11.6	Neutral

Stock performance (1 year)



Financials and Valuation

Income Statement		(INR Million)			
Y/E March	2012	2013E	2014E	2015E	
Gross Sales	69,558	82,475	89,094	102,028	
Change (%)	12.6	18.6	8.0	14.5	
Exports	36,920	45,527	46,973	54,011	
Net Domestic Sales	31,557	35,699	40,894	46,619	
Other Operating Income	1,730	1,765	1,870	1,982	
Net Income	70,207	82,991	89,737	102,612	
Change (%)	11.2	18.2	8.1	14.3	
Total Expenditure	53,619	61,032	67,366	77,044	
EBITDA	16,589	21,959	22,371	25,568	
Margin (%)	23.6	26.5	24.9	24.9	
Depreciation	3,122	3,125	3,375	3,658	
EBIT	13,466	18,835	18,996	21,909	
Int. and Finance Charges	383	175	97	97	
Other Income - Rec.	1,395	1,716	1,887	2,076	
PBT before EO Items	14,478	20,376	20,787	23,888	
Extra Ordinary Expense	0	0	0	0	
PBT but after EO Exp.	14,478	20,376	20,787	23,888	
Tax	3,036	4,890	4,989	5,733	
Tax Rate (%)	21.0	24.0	24.0	24.0	
Reported PAT	11,442	15,485	15,798	18,155	
Adj PAT	11,252	13,521	15,798	18,155	
Change (%)	16.3	20.2	16.8	14.9	
Margin (%)	16.0	16.3	17.6	17.7	

Balance Sheet		(INR Million)			
Y/E March	2012	2013E	2014E	2015E	
Equity Share Capital	1,606	1,606	1,606	1,606	
Reserves	74,694	87,082	98,931	112,547	
Revaluation Reserves	90	90	90	90	
Net Worth	76,389	88,778	100,626	114,243	
Loans	135	1,613	1,613	1,613	
Deferred Liabilities	2332	499	-1372	-3522	
Capital Employed	78,856	90,889	100,866	112,333	
Gross Block	46,321	51,321	55,821	60,321	
Less: Accum. Deprn.	14,111	17,236	20,611	24,269	
Net Fixed Assets	32,210	34,085	35,210	36,052	
Capital WIP	3,712	3,712	3,712	3,712	
Investments	12,688	12,688	17,688	21,188	
Curr. Assets	44,893	60,651	66,888	77,363	
Inventory	18,501	22,699	24,555	28,121	
Account Receivables	15,536	19,206	21,236	25,158	
Cash and Bank Balance	905	1,215	2,783	3,107	
Others	9,952	17,531	18,314	20,977	
Curr. Liability & Prov.	14,646	20,247	22,632	25,982	
Account Payables	14,646	20,247	22,632	25,982	
Net Current Assets	30,247	40,404	44,256	51,381	
Appl. of Funds	78,856	90,889	100,866	112,333	

E: MOSL Estimates

Ratios					
Y/E March	2012	2013E	2014E	2015E	
Basic (INR)					
EPS	14.0	16.8	19.7	22.6	
Cash EPS	17.9	20.7	23.9	27.2	
BV/Share	95.0	110.5	125.2	142.2	
DPS	1.7	3.3	4.2	4.8	
Payout (%)	14.3	20.0	25.0	25.0	
Valuation (x)					
P/E	28.9	24.0	20.6	17.9	
PEG (x)	1.8	1.2	1.2	1.2	
Cash P/E	22.6	19.5	17.0	14.9	
P/BV	4.3	3.7	3.2	2.8	
EV/Sales	4.6	3.9	3.6	3.2	
EV/EBITDA	19.6	14.8	14.5	12.7	
Dividend Yield (%)	0.4	0.8	1.0	1.2	
Return Ratios (%)					
RoE	14.7	15.2	15.7	15.9	
RoCE	18.8	22.6	20.7	21.4	
Working Capital Ratios					
Fixed Asset Turnover (x)	2.2	2.5	2.6	2.9	
Debtor (Days)	81	84	86	89	
Inventory (Days)	96	100	100	100	
Working Capital (Days)	153	172	169	172	
Leverage Ratio (x)					
Current Ratio	3.1	3.0	3.0	3.0	
Debt/Equity	0.0	0.0	0.0	0.0	

Cash Flow Statement		(INR Million)			
Y/E March	2012	2013E	2014E	2015E	
Op. Profit/(Loss) before T	16,589	21,959	22,371	25,568	
Interest/Dividends Recd.	1,395	1,716	1,887	2,076	
Direct Taxes Paid	-2,835	-6,724	-6,860	-7,883	
(Inc)/Dec in WC	4,456	-9,847	-2,284	-6,801	
CF from Operations	19,605	7,104	15,114	12,959	
EO expense	0	0	0	0	
CF from Oper. incl EO Expe	19,605	7,104	15,114	12,959	
(inc)/dec in FA	-5,245	-5,000	-4,500	-4,500	
(Pur)/Sale of Investment:	-6,784	0	-5,000	-3,500	
CF from Investments	-12,029	-5,000	-9,500	-8,000	
Issue of Shares	-81	0	0	0	
Inc/(Dec) in Debt	-5,584	1,478	0	0	
Interest Paid	-383	-175	-97	-97	
Dividend Paid	-1,633	-3,097	-3,949	-4,539	
CF from Fin. Activity	-7,682	-1,794	-4,046	-4,636	
Inc/Dec of Cash	-106	310	1,568	324	
Add: Beginning Balance	1,010	905	1,215	2,783	
Closing Balance	905	1,215	2,783	3,107	

N O T E S

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