

September 6, 2013

BSE Code: 500087 NSE Code: CIPLA Reuters Code: CIPL.NS Bloomberg Code: CIPLA:IN

Cipla Ltd, established in 1935, offers over 100 APIs and wide portfolio in excess of 1,000 drug formulations to over 170 countries worldwide. With a turnover of over \$1.5bn, the company is best known for its uncompromising quality standards in all products and services globally and has ~100 projects in its development pipeline including novel combinations and generics.

### Investor's Rationale

Cipla has filed 6 ANDAs with USFDA in FY'13 and 23 ANDAs are under registration. It has received 20 products back from its partners and is likely to market them on its own. The company has commercialized 47 products through its partners in the US and has developed 10 inhalers of which four have been launched in Europe. The drug major in its expansion spree to attain its next phase of growth is closely looking at emerging markets like China, Brazil, Russia and Turkey.

The company has achieved a remarkable milestone by acquiring Medpro in South Africa valued at ~₹27.0 bn. With this nurturing deal, Cipla will strengthen its position in South Africa and also expand its activities in other parts of Africa. Besides, the company has established strong presence in Uganda and is expanding its base in Algeria and Morocco as part of its North African thrust. We firmly expect that the company after the deal will compete more effectively using each-others strength in the dynamic local as well as global pharmaceutical environment.

The new drug pricing policy, ordering pharma companies to slash cost of some of their medicines, has put major drug makers under pressure and Cipla being a leader player is no exception to save itself from the heat. Cipla strongly against the policy believes that the new rule will adversely impact company's revenue by 2-3% in 2014.

Cipla witnessed an impressive performance in Q1FY'14, posting a 16.7% YoY increase in domestic sales at ₹11.32 bn, primarily on the back of rise in revenue from the anti-asthma, anti-biotics/infectives, and cardiovascular therapy segments. Further, exports of formulations registered a growth of 27.7% YoY to ₹10.34 bn, while exports of APIs fell by 13.1% YoY to ₹1.46 bn.

Recently, Cipla has launched the first bio similar of Etanercept in India; under the brand name 'ETACEPT' for the treatment of rheumatic disorders. The management is confident that the introduction of its first biosimilar at lower cost will enable access of this drug to a greater number of patients in India, hence increasing the revenue base of Cipla.

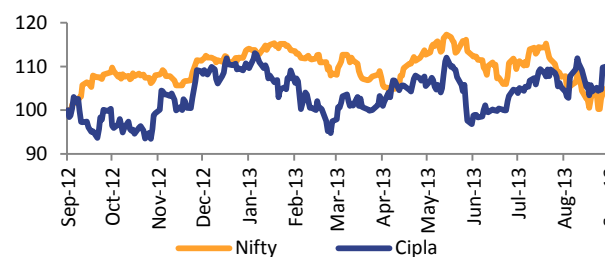
### Market Data

<b>Rating</b>	<b>BUY</b>
<b>CMP (₹)</b>	437.6
<b>Target (₹)</b>	<b>520</b>
<b>Potential Upside</b>	~18.8%
<b>Duration</b>	Long Term
Face Value (₹)	2
52 week H/L (₹)	440.8/320.3
Adj. all time High (₹)	557.8
Decline from 52WH (%)	0.7
Rise from 52WL (%)	36.6
Beta	0.5
Mkt. Cap (₹bn)	351.3
Enterprise Value (₹bn)	354.3

### Fiscal Year Ended

Y/E	FY12A	FY13A	FY14E	FY15E
Revenue (₹bn)	71.6	85.0	97.7	111.2
EBITDA (₹bn)	18.0	24.2	26.5	28.7
Net Profit (₹bn)	11.4	15.4	17.0	18.3
Adj EPS (₹)	14.3	19.2	21.1	22.8
P/E (x)	30.7	22.7	20.7	19.2
P/BV (x)	4.6	3.9	3.3	2.9
EV/EBITDA (x)	19.3	14.6	13.3	12.2
ROCE (%)	18.2	20.1	18.9	18.1
ROE (%)	15.0	17.1	16.1	15.0

### One year Price Chart



### Shareholding Pattern

	Jun'13	Mar'13	Diff.
Promoters	36.80	36.80	-
FII	23.11	23.89	(0.78)
DII	10.81	10.19	0.62
Others	29.28	29.12	0.16

*Cipla has around 5,500 drugs under its portfolio which includes prescription drugs for all kinds of ailments - arthritis, cancer, and depression as well as over-the-counter drugs for cold, oral hygiene, and skin care.*

*Roughly 40% of HIV/AIDS patients undergoing antiretroviral therapy worldwide take Cipla drugs.*

**Cipla Ltd - one of the world's largest generic pharmaceutical companies with a presence in over 170 countries**

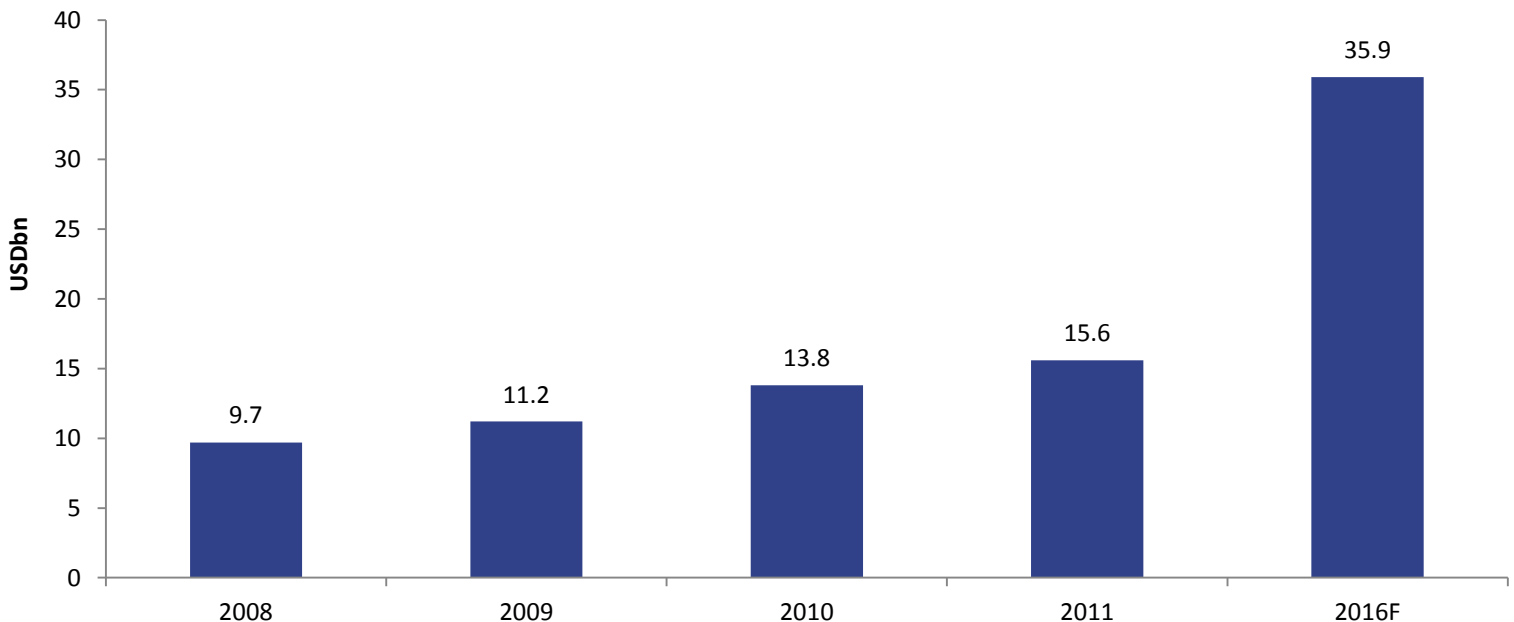
Cipla Ltd (CIPLA), an India based pharmaceutical manufacturing company with presence in over 170 countries, was founded as The Chemical, Industrial, & Pharmaceutical Laboratories, in 1935. The company offers various drugs and healthcare products. It has around 5,500 drugs under its portfolio which includes prescription drugs for all kinds of ailments -arthritis, cancer, depression as well as over-the-counter drugs for cold, oral hygiene, and skin care. It operates through its 8 manufacturing plants located throughout the country. Over the past 77 years, Cipla has emerged as one of the most respected pharmaceutical names, not just in India but worldwide.

Over the years, Cipla's several dosage forms and APIs continued to enjoy the approval of major international regulatory agencies. Being the world's largest manufacturer of antiretroviral drugs (ARVs) to fight HIV/AIDS, roughly 40% of HIV/AIDS patients undergoing antiretroviral therapy worldwide take Cipla drugs. Further, Cipla has been able to imprint a significant presence in the international market. It is evaluating several business models such as capturing value through direct presence in key priority markets including South Africa, US, Europe and Australia. On domestic front, the company has delivered robust growth across therapies and has maintained its leadership position in respiratory, urology and HIV.

Recently, the company has acquired 100% stake of the South African drug-maker, Cipla Medpro, taking an important step towards consolidating its international business. The investment was aimed at further strengthening the company's commitment to the African continent. With this acquisition, South Africa will become the second largest drug market for Cipla.

The pharmaceutical major witnessed a robust performance in FY'13. The company registered a growth in its revenue from operations, up by 17% YoY, at ₹82.95 bn as against ₹70.75 bn, in the same period a year ago. Further, operating margins increased by 34% YoY on the back of reduction in material cost on account of improved realisations, changes in the product mix and higher contribution of Escitalopram in the US.

**Revenue of Indian pharmaceuticals industry is expected to reach USD 35.9 bn by 2016**



Source : IBEF

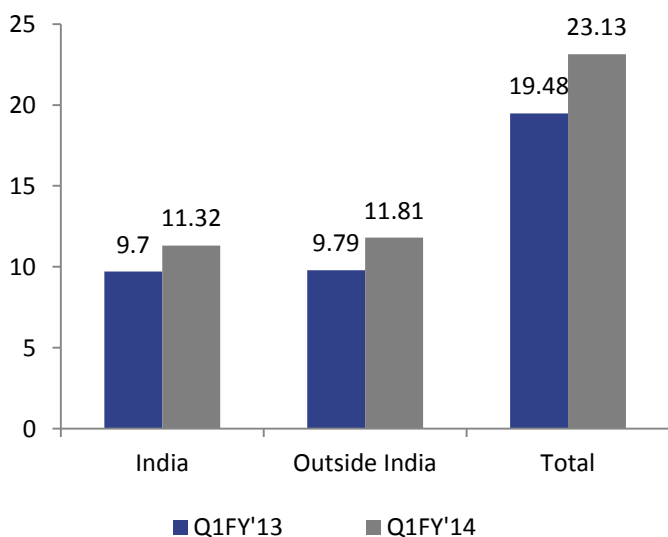
### Witnessed strong numbers in Q1FY'14

**Domestic business grew in line with expectations:** The drug maker registered a strong performance in Q1FY'14, as the company posted a growth of more than 25% in income from operations. On domestic front, sales grew 16.7% YoY to ₹11.32 bn in Q1FY'14 primarily on the back of growth in anti-asthma, anti-biotics/infectives, and cardiovascular therapy segments. Over the long term, it can be expected that the company would grow ahead of the industry growth, which rose by a healthy 10% in FY'13, despite of the fragile economic environment.

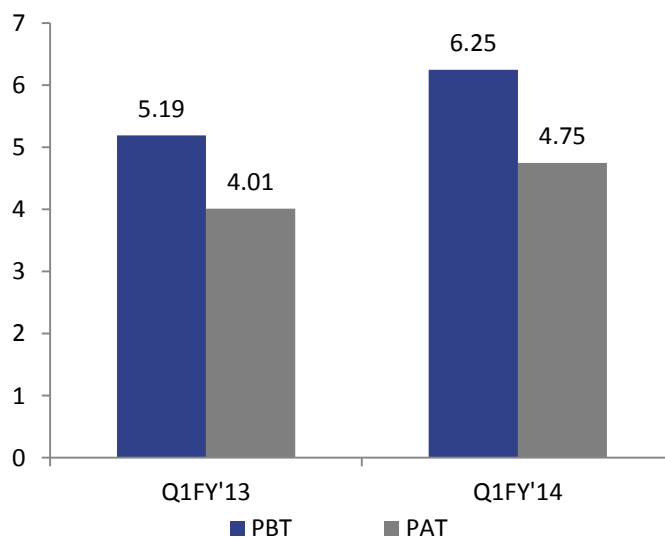
**Exports of formulations rose 27.7%, on growth in various segments:** During Q1FY'14, the company's export of formulations witnessed a solid rise in revenue by 27.7% YoY to ₹10.34 bn, primarily due to growth in anti-retroviral, anti-asthma and anti-allergic segments. While, exports of APIs declined by 13.1% YoY to ₹1.46 bn.

Domestic sales surged 16.7% YoY to ₹11.32bn, while exports grew by 27.7% YoY to ₹10.34 b, during Q1FY'14.

#### Sales Growth (in ₹bn)



#### Growth in Profits (in ₹bn)



Cipla witnessed a decent growth in operating margin during Q1FY'14, as it grew 24.8% YoY to ₹6.75 bn.

Cipla has challenged the government's new drug pricing order. Giving the relief, the court had asked the firm to supply the revised price list of regulated medicines to its distributors, suppliers and retailers.

**EBITDA margin expanded 24.8% YoY:** The company's EBITDA margin grew modestly by 24.8% YoY to ₹6.75 bn in Q1FY'14 against ₹5.41 bn in Q1FY'12. For FY'13, Cipla reported a robust growth in its margins at 28.5% against 23.6% in FY'12. We expect that the company will be able to maintain its margin going ahead due to expected normalcy in the domestic business after the application of NPPP provisions. Cipla's domestic margin is likely to improve with higher capacity utilization at Indore SEZ (capex ₹3.0 bn) coupled with the weakening of the local currency.

### DPCO to impact the growth by 2-3% in 2014

With the Drug Prices Control Order (DPCO) 2013 coming into effect, issued by the National Pharmaceutical Pricing Authority (NPPA), slashing the prices of 151 medicines, out of 348 drugs that are listed under the National List of Essential Medicines (NLEM). The new drug pricing policy, being effective from July 29, has ordered pharma companies to slash cost of some of their medicines and the decreased prices are made effective on the drugs which are already in the market, within 45 days

*The company plans to increase its focus on domestic markets with new therapies such as oncology and neuro-psychiatry in the coming future.*

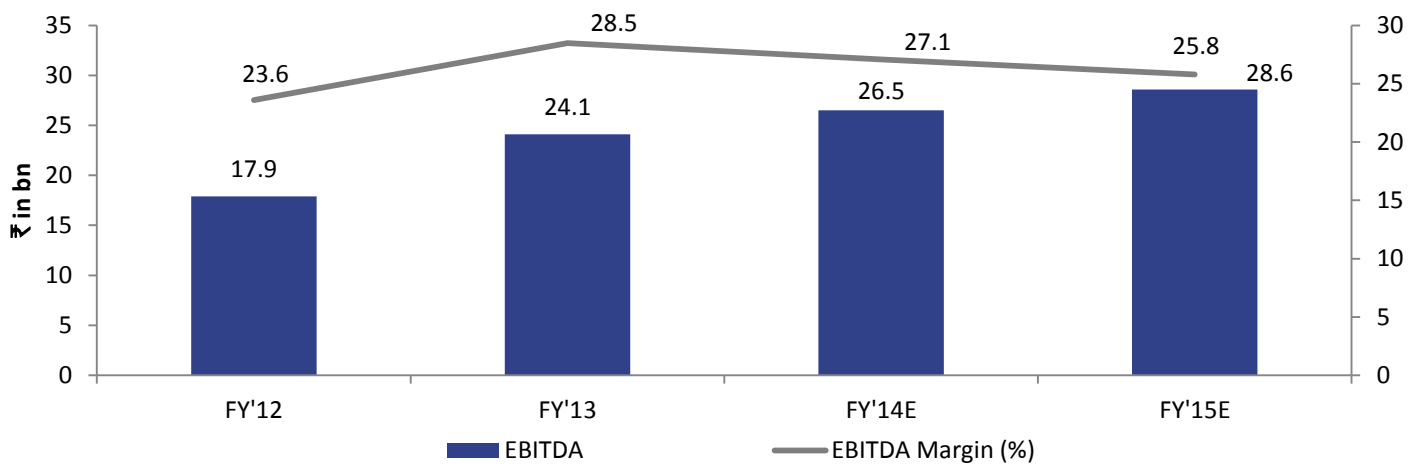
of the notification being issued. This has put major drug makers under pressure and Cipla being a leader player is no exception to save itself from the heat. Cipla strongly against the policy believes that the new rule will adversely impact company's revenue by 2-3% in 2014. However, the order is likely to bring some cheer on the face of the patients as there is a major shift from cost-based to market based pricing methodology under the new policy.

Cipla has challenged the government's new drug pricing order asking it to reduce prices of its 125 drugs within 45 days of issuance of the notification. Giving the relief, the court had asked the firm to supply the revised price list of regulated medicines to its distributors, suppliers and retailers.

### Increasing penetration in the domestic market to drive growth

Being one of the dominant player in the domestic market having presence in formulations and bulk drugs manufacturing, the company enjoys a market share of ~5%, contributing 47% to the total turnover in FY'13. The company's enjoys a very strong foothold with chemists and doctors alike and has one of the biggest brand portfolios supported by a field force of ~7,500 MRs. The company plans to increase its focus on domestic markets with new therapies such as oncology and neuro-psychiatry in the coming future. Cipla plans to focus on growing its market share and sales by increasing penetration in the Indian market, especially in rural areas, and plans to expand its product portfolio by launching biosimilars, particularly relating to the oncology, anti-asthmatic and anti-arthritis categories.

### EBITDA trend to stay elevated



### Strong ANDAs product pipeline

The company has filed 6 ANDAs with USFDA in FY'13 and 23 ANDAs are under registration. Cipla has received 20 products back from its partners and is likely to market them on its own. The company has commercialized 47 products through its partners in the US and has developed 10 inhalers of which four have been launched in Europe. The drug major in its expansion spree to attain its next phase of growth is closely looking at emerging markets like China, Brazil, Russia and Turkey.

*Cipla has filed for a generic version of Seretide inhaler in the EU, which, if approved, has the potential to add \$200 mn per annum to the company's revenues.*

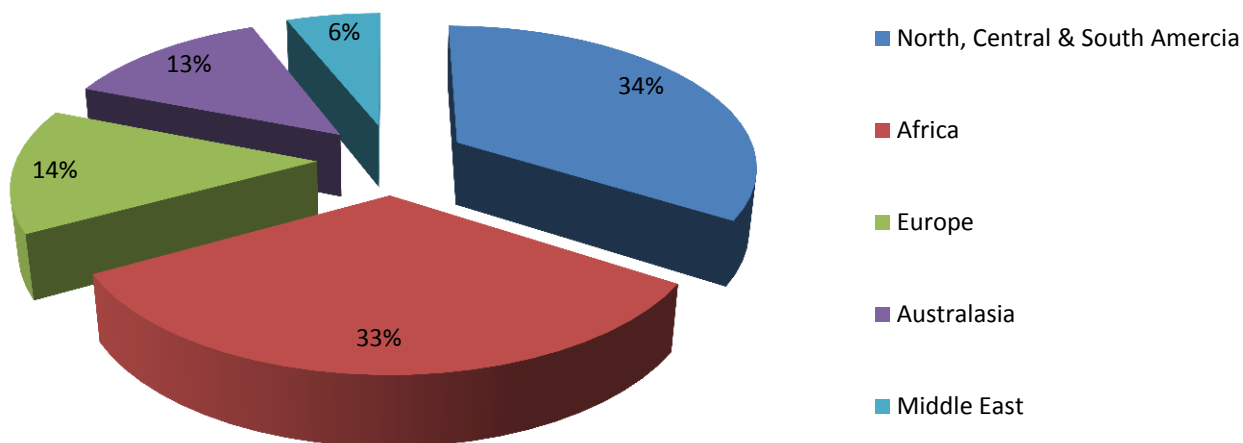
*Dymista being an innovative drug, the margins are expected to be very healthy, which may lift the company's overall profitability*

### Changes in export strategy and multiple triggers like Dymista (US) ramp up, EU inhaler launch may boost profitability

Cipla has traditionally adopted a partnership model to sell its drugs in the overseas markets. But now, the company has outlined its intent to make some fundamental shifts in strategy. The leading pharma company now plans to establish direct presence in key export markets by setting up its own distribution channel. Moreover, it intends to consciously scale down its low-margin anti-retroviral sales and instead focus on profitable products.

The company is also looking at gaining its own foothold in key regulated markets such as the US and Europe. But, given the competition in these markets, the company may have to adopt an inorganic strategy to scale up front end presence in the regulated markets. Even as the domestic market may continue to provide steady cash flow to Cipla, the bigger upside for the company may accrue from its proposed inhaler launches in the European markets. Recently, the company has filed for a generic version of Seretide inhaler in the EU, which, if approved, has the potential to add \$200 mn per annum to the company's revenues. Further, collaboration with Swedish generic maker, Meda pharma will allow the drug maker to expand exclusive rights to the patented drug Dymista, its nasal treatment for allergic rhinitis, which will further help in expanding the revenue base. Dymista being an innovative drug, the margins are expected to be very healthy, which may lift the company's overall profitability.

**Export market division (FY'13)**



*The company's management is confident for the growth from the acquisition and has projected a growth for generic drugs of ~14% per year for the next several years.*

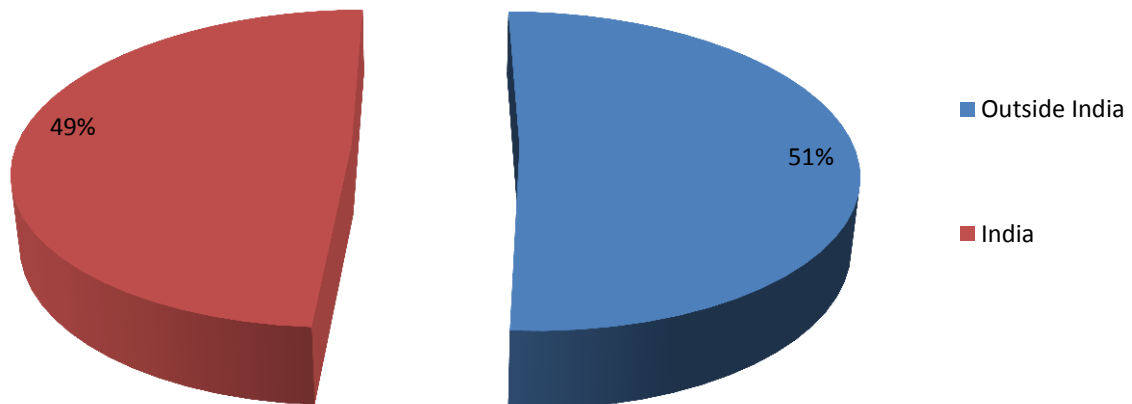
### Medpro acquisition to strengthen Cipla's presence in South Africa

Cipla Ltd, one of India's leading generic pharmaceutical companies is likely to get a strong foothold in South Africa with the acquisition of 100% stake in Cipla Medpro South Africa Ltd, a leading provider of chronic medicines to the South African market, for an aggregate consideration of ₹27.07 bn. The company's management is confident for the growth from the acquisition and has projected a growth for generic drugs of ~14% per year for the next several years. Cipla and Medpro have enjoyed a

*The company aims to build a robust portfolio of differentiated products to drive growth in developed markets.*

long-standing symbiotic relationship spanning two decades. The management is confident that the integrated business will compete more effectively in the changing local and global pharmaceutical environments and as such there will be an increasing focus on key African markets. Moreover, patients and the healthcare landscape will benefit both from Cipla's 77+ years of experience in cross products, technologies, dosage forms and Cipla's philosophy of striving hard to provide greater access to medicine. Further, the company will leverage the broad spectrum of products in its domestic market to optimally capitalise across other emerging countries. Moreover, it aims to build a robust portfolio of differentiated products to drive growth in developed markets. Recent achievements of regulatory approval for Fluticasone HFA in several European countries and commercialisation of Azelastine combinations with Meda AB are few examples in this direction.

### Geographical sales break-up (Q1FY'14)



*Some of the Cipla's brands and therapy segments are facing stiff competition from new innovative products of the competitors.*

### Key Concerns

- The Indian Pharmaceutical industry, being highly fragmented, is very competitive. Some of the Cipla's brands and therapy segments are facing stiff competition from new innovative products of the competitors. Hence, there are challenges in sustaining leadership positions in therapy segments. However, the company has been very active on innovation front to mitigate such challenges.
- The company has some pending legal cases on account of alleged overcharging in respect of certain drugs under the Drug Price Control Order (DPCO). Any unfavourable outcome in these proceedings could have an adverse impact on the company.

**Balance Sheet (Consolidated)**

Y/E (₹mn)	FY12A	FY13A	FY14E	FY15E
Share Capital	1,605.8	1,605.8	1,605.8	1,605.8
Reserve and surplus	74783.5	88581	103,930.1	120,297.3
<b>Net Worth</b>	<b>76,389.3</b>	<b>90,186.8</b>	<b>105,535.9</b>	<b>121,903.1</b>
Loan	134.5	9,669.3	9,669.3	9,669.3
Long term provisions	2,524.6	2,823.7	3,106.1	3,478.8
Current Liabilities	11,817.0	10,792.5	9,713	9,713
Net Deferred Tax Liability	2,332.4	2,805.4	2,805.4	2,805.4
Other long term liabilities	300.00	300.0	300	300
<b>Capital Employed</b>	<b>93,497.8</b>	<b>116,577.7</b>	<b>131,130.0</b>	<b>147,869.9</b>
Fixed assets	35,866.60	39,877.60	43,865.4	48,251.9
Investments	12,691.1	25,324.4	25,324.4	25,324.4
Loans and Advances	9405.4	9,312.6	11,469.6	13,734.4
Current Assets	35,481.0	42,012.0	50,414.4	60,497.3
Other Assets	53.7	51.1	56.2	61.9
<b>Capital Deployed</b>	<b>93,497.8</b>	<b>116,577.7</b>	<b>131,130.0</b>	<b>147,869.9</b>

**Key Ratios (Consolidated)**

Y/E	FY12A	FY13A	FY14E	FY15E
EBITDA Margin (%)	25.1	28.5	27.1	25.8
EBIT Margin (%)	20.8	25.0	23.6	22.5
NPM (%)	16.0	18.2	17.4	16.5
ROCE (%)	18.2	20.1	18.9	18.1
ROE (%)	15.0	17.1	16.1	15.0
Adj EPS (₹)	14.3	19.2	21.1	22.8
P/E (x)	30.7	22.7	20.7	19.2
BVPS (₹)	95.1	112.3	131.4	151.8
P/BVPS (x)	4.6	3.9	3.3	2.9
EV/Operating Income (x)	4.9	4.3	3.7	3.2
EV/EBITDA (x)	19.3	14.6	13.3	12.2
EV/EBIT (x)	23.3	16.6	15.3	14.1

**Profit & Loss Account (Consolidated)**

Y/E (₹mn)	FY12A	FY13A	FY14E	FY15E
<b>Total Income</b>	<b>71,602.3</b>	<b>85,014.7</b>	<b>97,655.8</b>	<b>111,229.9</b>
Expenses	53,619	60,815	71,153.3	82,537.8
<b>EBITDA</b>	<b>17,983.7</b>	<b>24,199.9</b>	<b>26,502.5</b>	<b>28,692.1</b>
Depreciation	3122.2	3304.8	3,503.1	3,713.3
Exceptional Items	0.0	397.7	0.0	0.0
<b>EBIT</b>	<b>14,861.5</b>	<b>21,292.8</b>	<b>22,999.4</b>	<b>24,978.8</b>
Interest	383.4	339.1	542.6	705.3
Profit Before Tax	14,478.1	20,953.7	22,456.9	24,273.5
Tax	3065.1	5443.1	5,501.9	5,947.0
Profit after Tax	11,413.0	15,510.6	16,954.9	18,326.5
Minority Interest	29.4	(62.1)	-	-
<b>Net Profit</b>	<b>11,442.4</b>	<b>15,448.5</b>	<b>16,954.9</b>	<b>18,326.5</b>

**Valuation and view**

Despite the tough business environment, Cipla has posted strong numbers in Q1FY'14 on robust performance showed by local and foreign markets. Besides, the overall changing healthcare scenario has necessitated Cipla to give impetus to international business like Africa, Europe, Australia etc. and currently all are running successfully. On regulatory front also, to boost the overall sector's growth government has stepped in and allowed 100% FDI approvals in pharma sector. Besides, in budget 2013-14, the government has further given a nod for 15% investment on new plant and machinery which is likely to raise the investments in new projects and at the same time provide tax benefit. Thus, we believe that the company's individual effort as well as the support provided by the government will surely help the drug manufacturer to maintain the growth trajectory.

At a current market price (CMP) of ₹437.6, the stock trades at 21.1x FY14E and of 22.8x FY15E, earnings. We recommend 'BUY' with a target price of ₹520, which implies potential upside of ~18.8% to the CMP from 1 year perspective.



Indbank Merchant Banking Services Ltd.  
I Floor, Khiviraj Complex I,  
No.480, Anna Salai, Nandanam, Chennai 600035  
Telephone No: 044 – 24313094 - 97  
Fax No: 044 – 24313093  
[www.indbankonline.com](http://www.indbankonline.com)

#### Disclaimer

@ All Rights Reserved

This report and Information contained in this report is solely for information purpose and may not be used as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. The investment as mentioned and opinions expressed in this report may not be suitable for all investors. In rendering this information, we assumed and relied upon, without independent verification, the accuracy and completeness of all information that was publicly available to us. The information has been obtained from the sources that we believe to be reliable as to the accuracy or completeness. While every effort is made to ensure the accuracy and completeness of information contained, Indbank Limited and its affiliates take no guarantee and assume no liability for any errors or omissions of the information. This information is given in good faith and we make no representations or warranties, express or implied as to the accuracy or completeness of the information. No one can use the information as the basis for any claim, demand or cause of action.

Indbank and its affiliates shall not be liable for any direct or indirect losses or damage of any kind arising from the use thereof. Opinion expressed is our current opinion as of the date appearing in this report only and are subject to change without any notice.

Recipients of this report must make their own investment decisions, based on their own investment objectives, financial positions and needs of the specific recipient. The recipient should independently evaluate the investment risks and should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document and should consult their advisors to determine the merits and risks of such investment.

The report and information contained herein is strictly confidential and meant solely for the selected recipient and is not meant for public distribution. This document should not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced, duplicated or sold in any form.